The Southland Corporation Annual Report -- 1981
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THE SOUTHLAND CORPORATION • 1981 ANNUAL REPORT



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Financial Highlights

(Dollars in thousands except per share data)

	Year Ended December 31		
For the Year	1981	1980	% Change
Total Revenues	$5,734,160	$4,782,605	19.9
Net Earnings	94,191	76,052	23.9
Primary Earnings Per Share*	3.98	3.22	23.6
Diluted Earnings Per Share	3.86	3.13	23.3
Cash Dividends	24,859	21,511	15.6
Return on Beginning Shareholders' Equity	17.3%	15.5%	
At Year-End			
Working Capital	135,626	174,966	(22.5)
Current Ratio	1.27	1.44	
Long-Term Debt	320,918	312,535	2.7
Shareholders' Equity	615,021	544,705	12.9
Book Value Per Share*	25.98	23.04	12.8
Annual Dividend Rate Per Share	1.08	.96	12.5
Average Shares Outstanding (000's)	23,676	23,640	.2
Number of Shareholders	7,336	8,429	(13.0)
Number of Employees	49,600	46,800	6.0

*Based on average number of shares outstanding during the period after adjusting for all stock dividends.



THE SOUTHLAND CORPORATION, originator of the convenience store concept, is one of the leading specialty retailers in the United States. Its activities are grouped into three business segments.

THE STORES GROUP is the world's largest operator and franchisor of convenience stores, with 7,002 7-Eleven stores in 42 states, the District of Columbia and five provinces of Canada, as well as 97 Gristede's and Charles & Co. food stores and sandwich shops in metropolitan New York and 35 Super-7 multi-pump self-serve gasoline outlets. The Group also includes a gasoline supply division, four merchandise distribution centers and six fast food production facilities serving 7-Eleven and other customers.

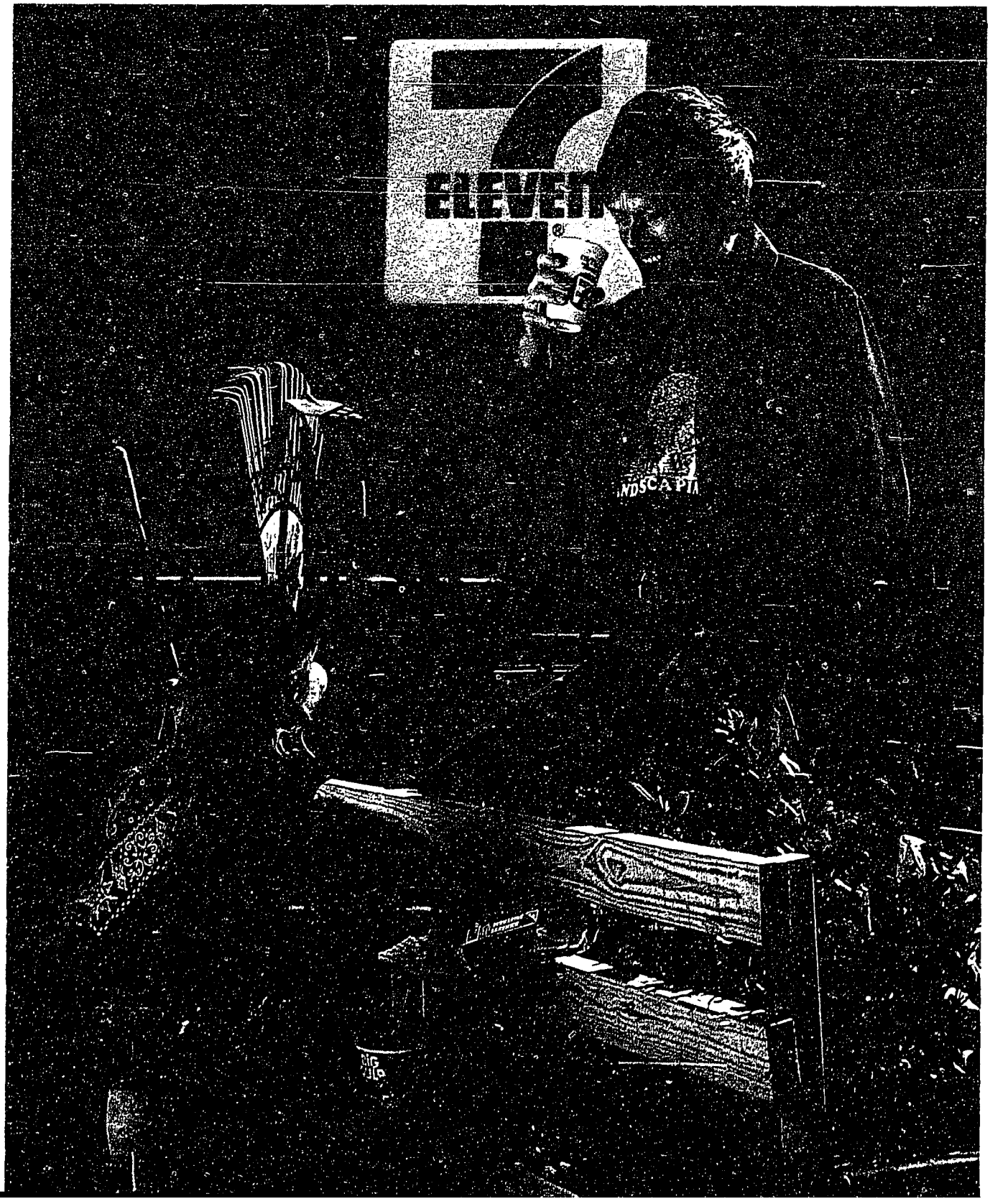
The Company has equity interests in 346 R S McColl confectionery, tobacco and news (CTN) stores and 16 7-Eleven units in the United Kingdom, 17 Närköppet and 16 7-Eleven stores in Sweden, and 18 Super Siete convenience stores in Mexico. An additional 426 7-Eleven stores are operated by area licensees in the United States, 1,247 in Japan, 46 in Taiwan, 40 in Australia, 15 in Canada and 8 in Hong Kong.(1)

THE DAIRIES GROUP is one of the nation's major processors of dairy products, which are marketed under 12 well-known regional brand names in 42 states, the District of Columbia and Canada.

THE SPECIAL OPERATIONS GROUP includes Chief, which operates 266 retail auto parts stores, as well as the Chemical, Reddy Ice and Tidel Systems Divisions.

(1) Sales of these operations are not reported in Southland's Total Revenues, while equity in earnings of affiliates and royalties from area licensees are included.

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TO OUR SHAREHOLDERS:



JOHN P. THOMPSON JERE W. THOMPSON

1981 was the 24th consecutive year Southland achieved record revenues and earnings. It was a year of solid growth accomplished in the most difficult business environment since the mid-'70s. Net earnings reached $94.2 million, up 23.8% on a 19.9% gain in revenues to $5.73 billion, up almost $1 billion. Primary earnings per share for the year increased 23.6% to $3.98, and fully diluted earnings rose 23.3% to $3.86 a share.

Sales of 7-Eleven, our principle business, were strong throughout the year, up 19.1% to $4.73 billion. Merchandise sales in stores open over 12 months were up more than 13% from the prior year, well ahead of the rate of inflation in the product mix. Although the percentage gain in sales slowed somewhat in the last half, the rate of inflation also showed a similar decline. This resulted in relatively stable real growth in 7-Eleven sales throughout the year.

To support this excellent growth trend, Southland has developed the most aggressive multi-media advertising and marketing program in the Company's history. Our new theme, "America Likes The Freedom of 7-Eleven," was introduced this January on all three major television networks. The program promotes the hassle-free, time-saving personal freedom of shopping for sound consumer value at 7,000 neighborhood 7-Eleven stores.

Self-serve gasoline sales increased 30.9% in 1981 and exceeded $1 billion for the first time. Since gasoline now represents one-fourth of total convenience store sales, we recently formed a gasoline supply division whose primary purpose is to purchase and provide this product to the 7-Eleven retail operations.

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The division is expected to supply, either directly or through exchange arrangements, a majority of 7-Eleven's requirements. In addition, it has allowed the Company to expand its wholesale business significantly, and we expect these activities to add materially to 1982 sales and earnings.

In August, Southland celebrated the tenth anniversary of its distribution system designed to serve the unique requirements of 7-Eleven. Sales and profits from the four regional Centers were well ahead of 1980, even though the newest one has not reached a profitable sales level due to the severely depressed economy of the Midwest area that it serves.

Dairies Group sales were up 2.7% to $368.2 million, while operating profits were down 2.5% from last year's all-time high, after excluding a nonrecurring gain in 1980. These results reflect a substantial reduction in government-sponsored school lunch and other social feeding programs, as well as highly competitive market conditions industry-wide.

Although Chief Auto Parts showed a strong upward sales trend throughout the year, its operating loss of $8.2 million was disappointing. Costs associated with more than doubling the number of stores in two years, as well as extensive remerchandising of the stores and warehouses, were primarily responsible for the loss. We expect considerable improvement in Chief's performance this year as the newer stores mature, the rate of openings is slowed, and the Division concentrates on increasing unit sales and profitability.

We strongly believe in the future of the convenience store business and intend to maintain our position of leadership. This commitment was demonstrated by record 1981 capital expenditures of $224 million, with almost three-fourths of the total invested in the Stores Group. At year-end, 7,400 retail outlets were in operation, including 7,002 7-Eleven and 266 Chief stores.

The 7-Eleven concept has been well accepted by consumers in every country where introduced. At year-end, area licensees in six countries were operating 1,782 7-Eleven stores. During 1981, 320 stores were opened, including 232 in Japan and 49 in the United States. A new license agreement was signed early last year for Belgium, the Netherlands and Luxembourg, and the first 7-Eleven in Amsterdam will open soon.

In February 1982, the annual cash dividend rate was raised to $1.16 per share, following the April 1981 increase to $1.08 from 96¢. Southland has increased the annual rate 11 times in the past 12 years, providing shareholders with a compound growth rate of 17.9%. The current cash dividend, as well as the discontinuance of the 3% stock dividend, reflects our policy to maintain the payout ratio between 25% and 30% of prior-year earnings.

The "Southland family" has enthusiastically supported a variety of national and community causes for many years. Employees, franchisees, shareholders, suppliers and customers have raised more than $21 million since 1976 for the Muscular Dystrophy Association. In 1978, the Dairies Group became the first national corporate sponsor of the March of Dimes and its "Mother's March on Birth Defects," and together with 7-Eleven, has sponsored the March of Dimes "WalkAmerica" since its beginning.

The Company is a major corporate sponsor of the 1984 Olympic Games in Los Angeles, and has funded an Olympic-class velodrome for cycling events. We also are a sponsor of the United States Olympic Committee's training program for American athletes preparing for the Games. As 1984 approaches, Southland will promote the Olympic spirit through television advertising and other marketing programs, and 7-Eleven stores will serve as Olympic information centers.

We are proud of the outstanding performance of our employees and franchisees during the past year and appreciate your confidence and support. Even though economic conditions remain uncertain, we are confident that Southland's inherent strengths provide the foundation for continuing growth.



John P. Thompson
Chairman



Jere W. Thompson
President

March 10, 1982

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STORES GROUP



(Millions)	1977	1978	1979	1980	**1981**	**5 Year Compound Growth**
Sales	$2,267.8	$2,784.0	$3,453.0	$4,294.1	**$5,199.3**	**22.9%**
Operating Profit	114.7	140.0	143.3	174.2	**221.6**	**19.4**

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Stores Group sales were up almost $1 billion to $5.20 billion, a 21.2% gain from $4.29 billion the prior year, and represented 91% of total Company sales.

7-Eleven sales were $4.73 billion, up 19.1%, with both merchandise and self-serve gasoline sales showing substantial increases. The merchandise sales gain in stores open 12 months or more substantially exceeded the rate of inflation in their product mix. Gasoline sales were well ahead of 1980 as gallonage continued to increase due to the larger number of 7-Elevens offering gasoline and increased market penetration.

7-Eleven Tops 7,000 Stores

Southland reached another milestone in its 54-year history with 7,002 7-Eleven stores at year-end, including 4,219 Company operated and 2,783 franchised, in 42 states, the District of Columbia and five provinces of Canada. During the year, 376 7-Elevens were opened and 269 closed as the Company continued to be more selective in choosing store locations. The vast majority of all new sites acquired are higher quality, more productive corner locations which, although more expensive, have greater long-term potential and improved return on investment.

Seven Million Shoppers

Almost seven million customers shop their neighborhood 7-Eleven every day, making an average purchase of $2.36. For them, it is a fast, easy-to-get-to store designed with their special needs in mind. 7-Eleven is their coffee shop, sandwich stop, juice bar, dairy store, soda fountain, gasoline station, newsstand ... all in one.

For most customers, "convenience" is the main reason they shop 7-Eleven. The stores are near their home or work; they save time and hassle with the fast in-and-out service; and they can buy the name-brand and Southland products they trust. Around-the-clock shopping is also an added convenience, since over 20% of 7-Eleven customers shop between 11 p.m. and 7 a.m. To accommodate those late-night customers, about 95% of all 7-Eleven stores stay open longer than the traditional 7 a.m. to 11 p.m., and 6,328 never close.

Averaging more than four trips a week, customers satisfy their needs from a selection of more than 3,000 items. They also provide a continuous stream of highly reliable market research data that is valuable in analyzing and refining the 7-Eleven product mix, as well as providing indicators of new trends in consumer demand.

And while 7-Eleven convenience appeals to people in every age group, over half come from the 85 million Americans who are between 25-54 years old. This segment is projected to increase to over 103 million by 1990, providing another 18 million potential customers.



Eric Heiden, winner of an incredible five individual gold medals in speed skating at the 1980 Winter Olympic Games, is serving as Southland's official spokesman for Olympic promotions and advertising. He is captain of the 7-Eleven cycling team now promoting bicycle racing. These Olympic contenders hope to compete in the 1984 Olympic cycling events which will be held in the velodrome funded by Southland.

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Self-Serve Gasoline Exceeds One Billion Gallons

To meet the needs of the neighborhoods they serve, an increasing number of 7-Eleven stores have added self-serve gasoline to their product mix. At year-end, gasoline was available at 2,517 locations, 271 more than the prior year, and accounted for 25.3% of 7-Eleven sales, up from 23.0% in 1980.

Southland strengthened its position as a leading independent retailer of gasoline in 1981, selling slightly over one billion gallons, including 956 million at 7-Elevens, up 20.6% from 1980. The 35 Super-7 high-volume gasoline units, located mainly on the West Coast, sold another 59 million gallons. Sales of these multi-pump stations are not included in 7-Eleven gasoline revenues. Although cents-per-gallon gross profit was slightly below 1980 due to the abundant supply, total gross profit dollars were up because of the higher gallonage sold.

In December, 1981, the Company formed a gasoline supply division, whose primary purpose is to purchase and provide a reliable supply of product to the 7-Eleven retail operations at the lowest possible cost. The division is expected to provide, either directly or through exchange arrangements, a majority of 7-Eleven's requirements nationwide.

Traffic-building self-serve gasoline is available at one-third of 7-Eleven stores nationwide. Last year, almost one billion gallons were sold.

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"America Likes The Freedom of 7-Eleven"

For over 50 years Southland has served the changing needs of its neighborhood customers by giving them what they want, when they want it, where they want it. And every day, Americans by the millions enjoy the freedom they find at 7-Elevens across the country.

A new theme, "America Likes The Freedom of 7-Eleven," was introduced through extensive network advertising in early 1982. The new marketing program will combine network and spot television, radio, and print advertising to emphasize both individual items and clusters of products that serve the special needs of customers. For example, breakfast items such as freshly brewed coffee and delicious 7-Eleven Danish pastry, "Egg Hamlette" or "Sausage and Biscuit" will be featured on morning radio programs to appeal to commuters. In the evenings, radio, television and newspaper advertising will feature repeatable staples, such as bread and milk, and emphasize 7-Eleven's competitive prices on these products. Other advertising, especially on network television, will highlight high-volume, high-margin items, such as fountain drinks and "Slurpee."

Training Programs Maximize "People Potential"

Because Southland's retail operations serve almost seven million customers a day, developing the "people potential" of employees and franchisees is important to the Company's continued success. Today, more than ever, the growing complexity of operating a 7-Eleven requires better qualified and motivated people who are supported by strong and effective management.

As part of that support, the Company has made a substantial investment in training programs which draw on field experience and utilize the latest classroom techniques. A good example, the "Certified Store Manager" program, introduced in 1979, emphasizes the development of management skills as the key to greater professionalism. Classroom instruction in general management principles, merchandising, inventory control, security and administrative procedures is followed by an in-store training and evaluation period.

New franchisees participate in a 10-day program at training stores where they study a wide range of basic store management skills—ranging from record keeping and merchandise ordering and receiving to customer relations and store maintenance. Franchisees then attend a week-long course in one of two Regional Training Centers. This is followed by an "In-Store Skills Development Program" to verify that they can use these skills in their own stores.

Southland's new marketing and advertising theme, "America Likes The Freedom of 7-Eleven," was introduced on all three television networks during the New Year's Day bowl games. The program emphasizes the hassle-free, time-saving personal freedom of shopping 7-Eleven.

Percent Convenience Store Sales (by Principal Product Category)

	1981	1980	1979	1978	1977
Gasoline	**25.3%**	23.0%	17.2%	13.4%	9.8%
Tobacco Products	**12.1**	12.3	12.9	12.9	14.2
Beer/Wine	**11.7**	11.7	12.4	12.9	13.7
Groceries	**11.5**	12.4	12.6	13.4	14.0
Soft Drinks	**10.0**	10.1	10.3	10.9	11.0
Non-Foods	**8.1**	8.0	8.7	9.4	9.9
Dairy Products	**6.3**	6.7	8.4	8.9	9.3
Other Food Items	**5.2**	5.6	6.2	5.5	4.7
Candy	**4.0**	4.0	4.3	4.7	5.0
Baked Goods	**3.2**	3.4	3.8	4.6	5.0
Health/Beauty Aids	**2.6**	2.8	3.2	3.4	3.4
Total	**100.0%**	100.0%	100.0%	100.0%	100.0%

The Company does not record sales by product lines but estimates the percentage of convenience store sales by principal product category based upon total store purchases.



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Major training programs also have been developed in response to specific operating needs. The "Shortage Control Program" was implemented using 7-Eleven field experience to provide a systematic method of controlling and reducing inventory shrinkage, or shortages. It has been extremely effective in accomplishing this goal. In addition, "Operation Alert" was developed to instruct store employees and franchisees in methods to minimize the potential for robberies or violence. The program is based on the successful "Robbery Prevention Program," which has substantially reduced incidences of robberies since its introduction in 1976.

Store Summary

	Opened	Closed	End of Year
7-Eleven			
United States	341	267	6,754
Canada	35	2	248
Total	376	269	7,002
Chief	79	29	266
Gristede's	4	7	97
Super Seven	0	2	35
Total	459	307	7,400
R S McColl — United Kingdom			
CTN	13	56	346
7-Eleven	0	0	16
Total	13	56	362
Affiliated Stores			
Sweden			
Näröppet	0	2	17
7-Eleven	4	1	16
Mexico			
Super Siete	8	0	18
Total	12	3	51
7-Eleven — Area Licenses			
Japan			1,247
United States			426
Taiwan			46
Australia			40
Canada			15
Hong Kong			8
Total			1,782

Gristede's Celebrates 90th Birthday

Gristede's 97 stores offer the greater New York area an extensive selection of premium-quality meats, fruits and vegetables, as well as a wide range of gourmet foods. Founded in 1891 to serve the carriage trade in Manhattan, Gristede's success through the years has been based on its quality products and personal services. Today, menu consultation, charge accounts and home deliveries are still individual touches provided at 47 stores. The Division includes 21 Charles & Co. sandwich shops and gourmet stores, which provide customers with an assortment of made-to-order sandwiches, delicatessen selections, specialty foods and gift-packaged delicacies.

International Strengthens Operations

R S McColl, a wholly-owned subsidiary operating both 7-Eleven and confectionery, tobacco and news (CTN) stores in the United Kingdom, continued to expand its product lines and improve the merchandising flexibility of its larger units. Included is a wider selection of staple grocery items, "Heat 'n Eat" fast foods, and non-foods such as toys, souvenirs and sporting goods. During the year, 13 units were added, 37 were remodeled, and 56 older, smaller locations were closed. A total of 346 CTN and 16 7-Eleven stores were in operation at year-end.

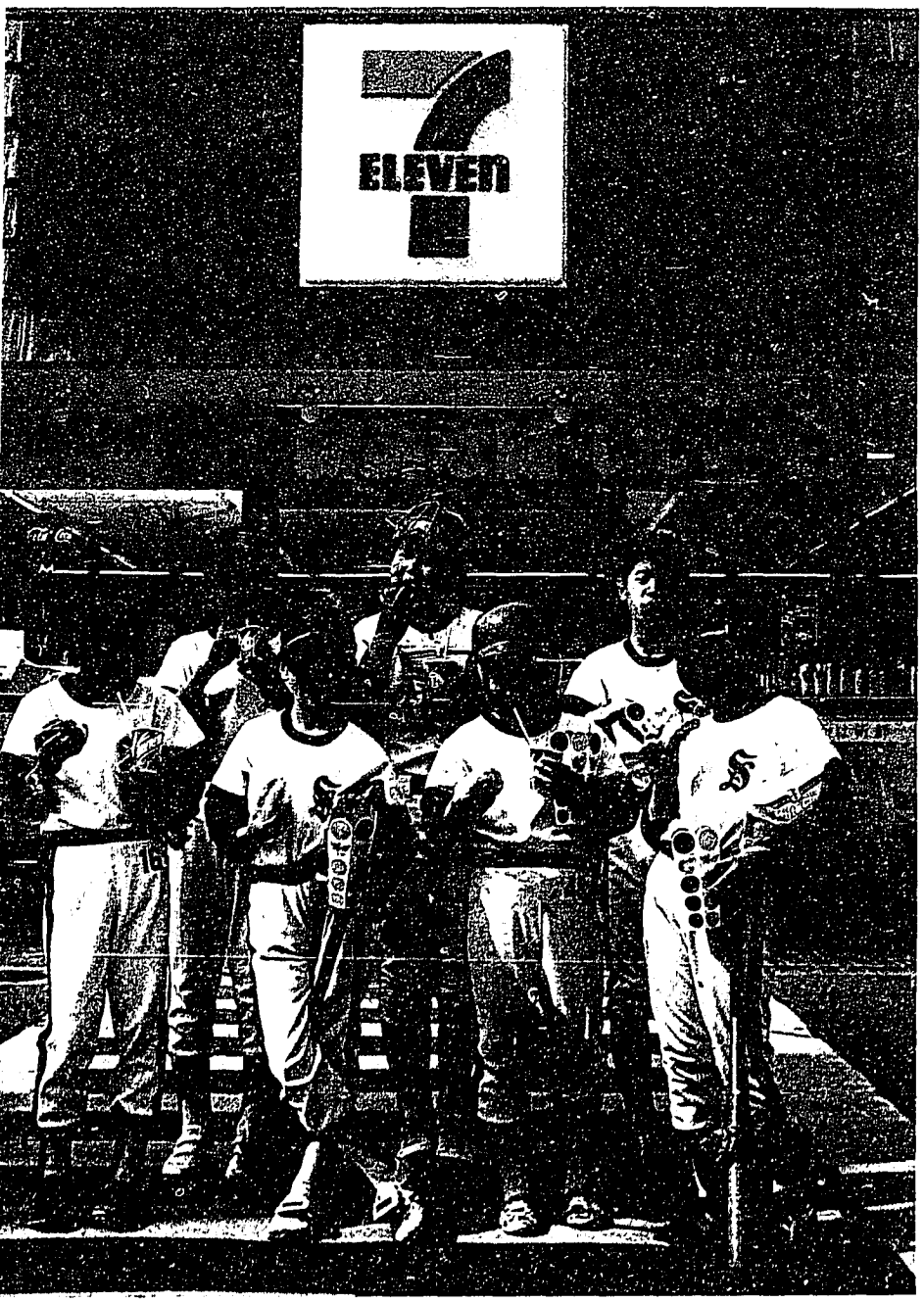
The Swedish subsidiary continued to introduce the 7-Eleven name in the Stockholm area, with six Näröppet units converted to 7-Eleven, four new stores added, and three closed. At the end of the year, 17 Näröppet and 16 7-Eleven stores were in operation.

In Mexico, Southland has an equity interest in 18 Super Siete convenience stores. During 1981, Super Siete entered the rapidly expanding Mexico City market with the opening of five units, while another three were added to the 10 in Monterrey.

7-Eleven Area Licensees Continue Expansion

The 7-Eleven concept continues to meet with success in each market entered through area licenses. The greatest development activity is in Japan, where 1,247 7-Elevens have been opened in only seven years, including 232 in 1981. This rapid addition of units, as well as steady sales growth, resulted in another outstanding year for Seven-Eleven Japan Co., Ltd.

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The other three licensees in the Pacific area also showed significant gains during the year. In Australia, 11 stores were opened, bringing the total to 39 in Melbourne and one in Sydney, a newly entered market. The licensee for Taiwan ended its second year with 46 stores, compared with 28 in 1980. The Hong Kong licensee opened its first 7-Eleven in April and completed the year with eight stores.

Southland's newest area licensee for Belgium, the Netherlands and Luxembourg will open its first 7-Eleven in Amsterdam in early 1982.

In North America, eight domestic area licensees for designated areas of 20 states opened 49 units, a 13% increase, to end the year with 426 stores. In the eastern Canadian provinces of New Brunswick, Nova Scotia and Prince Edward Island, 15 stores were in operation, as two were added during 1981.

Sales of international operations and area licensees are not included in Southland's revenues, while earnings of affiliates and royalties from licensees based upon sales are reported as other income.

The 7-Eleven area license concept has been enthusiastically accepted wherever introduced ... in the United States and five other countries. There are now 1,782 area-licensed 7-Elevens worldwide, including 1,247 in Japan.

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Fast Food Program Receives Major Award

Southland received the prestigious "Changemaker of the Year" award in 1981 from *Restaurants and Institutions,* a leading food service publication. The Company was recognized for identifying, developing and serving a new market for snacks and on-the-go meals through the coordinated efforts of its 7-Eleven stores and Food and Distribution Centers. The success of the program depends on a wide selection of high-quality products, many of which customers can easily heat in the stores' microwave ovens. Hot coffee, sandwiches and other fast food items now represent more than $250 million in sales, and when combined with sales of related items such as candy, snack foods and beverages, the total approaches $900 million.

Southland's six Food Centers produce an assortment of about 30 sandwiches, French bread pizzas and burritos, which are distributed to 7-Eleven and other customers nationwide. About one million gallons of flavored syrup for "Slurpee," the semi-frozen carbonated drink sold only in 7-Eleven stores, are also processed each year.

In addition, the Centers have introduced a line of sandwiches, burritos, and French bread and English muffin pizzas sized to fit vending machines. These products are marketed under the "Smileys Vend-Line" label. Also, the Salt Lake City facility has introduced a new item, the "Sandito" — either ham and cheese or barbecued beef wrapped in a flour tortilla — which has been extremely well received.

7-Eleven's convenient fast foods and fountain drinks are popular on-the-go, leisure-time snacks.

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Company Marks 10th Year of Distribution System

On August 2, Southland celebrated the tenth anniversary of the opening of its first Regional Distribution Center at Orlando, Florida. Three other Centers are located in Virginia, Illinois and Texas. With almost two million square feet of warehouse space, they serve customers in 33 states and the District of Columbia, including 4,643 or 66% of the 7-Eleven stores and almost 1,800 outside customers.

Total sales for the year increased 20.1% to $782.2 million, with operating profits up substantially from the prior year. The newest Center, opened in late 1979 near Champaign, Illinois, achieved the largest percentage sales gain, but due to economic conditions in the market area it serves, it has not yet reached a profitable level.

The Centers provide 7-Eleven stores with more than 50% of their merchandise requirements through a highly sophisticated and unique distribution system. The stores may order in less-than-case lots, and thereby better utilize shelf space, improve inventory turnover, stock fresher merchandise, and produce higher sales and profits from their limited selling area. They also provide the stores with greater flexibility to adjust product selections in response to customer preferences and seasonal demands, and to introduce new items and special promotions. The Centers achieved a 99% order fill rate for the eighth consecutive year.

Outside sales, primarily to food service accounts, including fast-food and sit-down restaurants, airlines, hospitals, schools and other industrial accounts, increased 79.8% to $130.9 million from $72.8 million in 1980. This substantial increase reflects a growing customer recognition of the many advantages provided by the Centers — ordering merchandise from a single supplier, reducing the time needed to order and check in merchandise, and consolidating deliveries and billings.

During the year, the Company developed a new electronic order entry system to provide outside customers with a more efficient ordering procedure. The system, to be implemented in early 1982, utilizes a specially-programmed, hand-held terminal in conjunction with the Distribution Centers' computerized order filling and delivery system. The customer uses a bar-coded product book and an electronic scanning wand to enter the order into the terminal. When the order is complete, the customer transmits the data via telephone to the appropriate Center, where the picking list is prepared. The order is then filled and assembled for the next scheduled delivery.

A new electronic order entry system, developed by the Distribution Centers for outside accounts, simplifies their merchandise ordering procedure. The customer utilizes a hand-held, programmed terminal, coded order book and electronic scanner.



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DAIRIES GROUP



(Millions)	1977	1978	1979	1980	**1981**	**5 Year Compound Growth**
Outside Sales	$235.9	$252.8	$313.9	$358.5	**$368.2**	**9.3%**
Intracompany Sales	125.8	135.6	158.6	175.2	**198.3**	**13.9**
Total	361.7	388.4	472.5	533.7	**566.5**	**10.8**
Operating Profit	5.8	6.1	9.7	14.0	**11.9**	**7.2**

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The Dairies Group, operating under 12 well-known regional brand names, serves customers in 42 states, the District of Columbia and Canada. With 27 processing plants and 83 distribution branches, the Group is a major supplier of milk, ice cream and related products, including yogurt, ultra-pasteurized creams, juices, eggnog, dips and toppings. The Dairies serve 5,709 7-Eleven stores, supplying about 69% of their dairy requirements.

Total sales were up 6.1% to a record $566.5 million, including intracompany sales of $198.3 million, a 13.2% gain. Outside sales increased 2.7% to $368.2 million, or 7% of Company sales. Operating profits were down 2.5% to $11.9 million from last year's record $12.2 million, after excluding a nonrecurring gain in 1980 of $1.8 million.

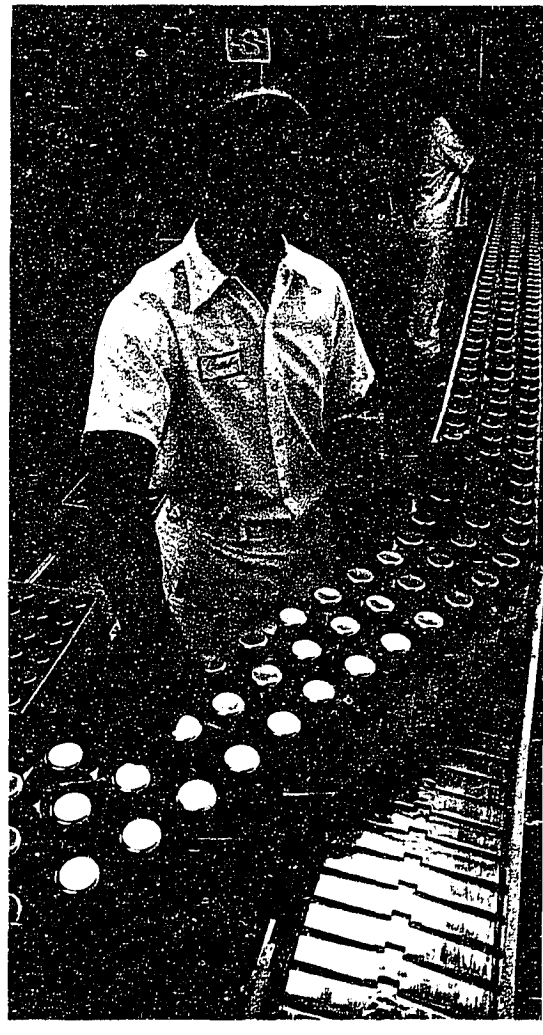
Adohr Farms • California
Bancroft • Wisconsin
Cabell's • Texas
Embassy • Maryland
Harbisons • Pennsylvania
Horten's • Ohio
Knowlton's • Texas
Merritt Foods • Missouri
Midwest Farms • Tennessee
Oak Farms • Texas
Specialty Products • Texas
Velda Farms • Florida
Wanzer's • Illinois

Sales Climate Changes
While sales were up due to the addition of new products and expansion of the Group's customer base, operating results reflected changes in market conditions that occurred during the year. Significant reductions in government-sponsored school lunch and other social feeding programs impacted the entire dairy industry, causing this market to decline about 18%, according to one industry study. As a result of these factors and other competitive conditions, prices could not be adjusted to recover higher production and distribution costs.

The Group, therefore, strengthened its marketing activities to replace the lost volume. Greater emphasis is being placed on commercial food service accounts and higher-margin dairy products, such as ice cream, frozen confections, cultured products and fruit juices.

Specialty Products Emphasized
The demand for premium-quality and low-fat dairy products, as well as frozen confections, has increased dramatically over the past few years. In response, the Dairies have expanded their production capacity for these profitable products.

In August, Southland purchased Merritt Foods Company, significantly increasing the Group's frozen novelty line and providing new distribution opportunities for other Group products. Merritt manufactures an extensive line of frozen novelties distributed throughout the United States and Canada, including the "Bomb Pop" and other frozen stick novelties, snow cones, and ice cream cups and sandwiches.



A wide assortment of fruit juices sold through 7-Eleven and to other customers is an increasingly important item in the Group's product line.

The Dairies Group has added the extremely popular "Bomb Pop" (facing page) to its line of frozen novelties.

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Also, other new dairy items added during the year are now being distributed to 7-Eleven and other customers in the western half of the country. Included are the "BIG Cone," a chocolate-lined cone of ice cream topped with chocolate and nuts, and the "BIG Neapolitan," a large ice cream sandwich filled with chocolate, vanilla and strawberry flavors. Embassy introduced "Barricini" all-natural, premium-quality ice cream in the metropolitan New York market in October, and plans to expand distribution along the East Coast in 1982.

The Group also continued to emphasize production of cottage cheese, yogurt, and other cultured products, as well as ultra-pasteurized coffee creamers, which are now used extensively in the 7-Eleven coffee program.

Juices and juice-based drinks continue to gain popularity. To meet this demand, the Dairies Group in 1981 began nationwide distribution of its "Farmfield" bottled juices. Its "Mission San Juan" all-natural, gourmet juice line is scheduled for national distribution in 1982. In addition, refrigerated orange juice in popular sizes of plastic, paper and glass containers is now produced by most of the Dairies Group.



The "Big Wheel" has been a popular ice cream novelty since its introduction in 1976.

Plant Improvements Add Capacity

A three-year program to expand capacity at the Velda Farms processing plant in Winter Haven, Florida, was begun in 1981. Serving one of the nation's fastest-growing markets, the facility will quadruple its processing capacity to 2 million gallons of milk a month when the project is completed. Also, Midwest Farms opened a distribution branch in Mobile, expanding its service into northern Florida and the Gulf Coast areas of Alabama and Mississippi. In California, the Tulare processing plant of Adohr Farms added yogurt and ultra-pasteurized cream production capacity to meet increasing demand on the West Coast.

As part of a program to reduce distribution costs and conserve energy, the Group is replacing a number of older gasoline-powered delivery trucks with fuel-efficient diesel models.

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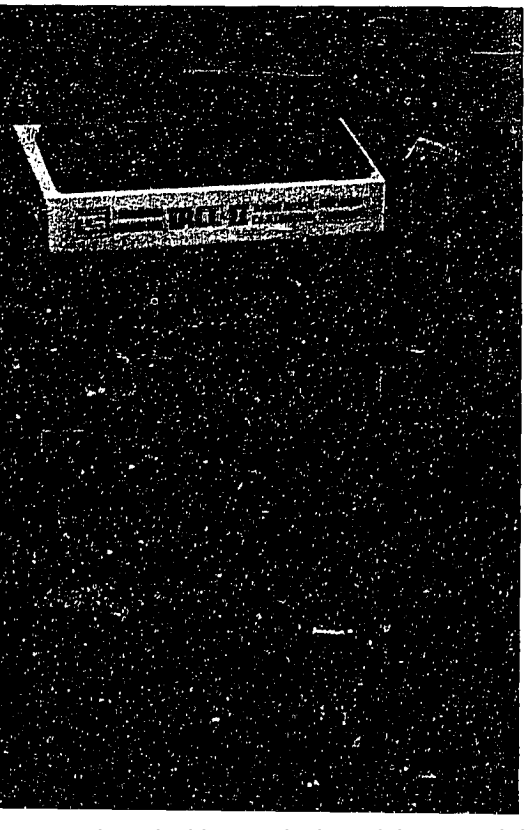
SPECIAL OPERATIONS GROUP



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(Millions)	1977	1978	1979	1980	**1981**	**5 Year Compound Growth**
Outside Sales	$32.4	$39.7	$ 89.3	$106.1	**$126.1**	**38.0%**
Intracompany Sales	14.5	15.3	23.2	16.2	**14.1**	**1.2**
Total	46.9	55.0	112.5	122.3	**140.2**	**29.5**
Operating Profit	6.6	5.6	7.4	(2.9)	**(9.3)**	—

The businesses included in the Special Operations Group sell products to a wide range of outside customers, as well as to other Southland divisions. Total sales of the Group were up 14.6% to $140.2 million, with outside sales increasing 18.9% to $126.1 million, or 2% of Company sales. The Group reported a $9.3 million operating loss, compared with a loss of $2.9 million a year ago. Costs associated with Chief's rapid store expansion, as well as its accelerated remerchandising program, resulted in an $8.2 million loss, compared with $2.7 million in 1980. Tidel Systems showed marked improvement during the year, with significantly higher outside sales and a reduction in its operating loss to $1.3 million from $2.0 million in 1980.



Tidel's TACC II cash dispensing system has substantially improved cash security in 7-Eleven stores.

Chief Accelerates Remerchandising Program

Chief Auto Parts, a major convenience retailer of automobile replacement parts, continued to expand its store operations in southern California and north Texas, two of the nation's fastest growing regions. A total of 79 stores were opened during the year and 29 closed, primarily because of relocations and lease expirations. At year-end, 266 stores were in operation, including 174 in California, 79 in Texas, 12 in Nevada and 1 in Arizona.

Automobile parts retailing continues to show great potential. As owners keep their cars longer, the need for repairs increases, and as service and repair costs escalate, they are performing more of the required maintenance. To improve service to this growing "do-it-yourself" market, Chief accelerated its remerchandising program to display more of the repair parts previously stored behind the counter, and added more accessories, impulse items and a wider selection of parts for imported cars.

Chief is slowing its rate of store openings and will concentrate on increasing unit sales and profitability. Also, its warehousing and distribution operations have been streamlined to achieve greater efficiencies and reduce costs. It is expected that these programs will significantly improve Chief's performance in 1982.

Tidel Increases Product Line

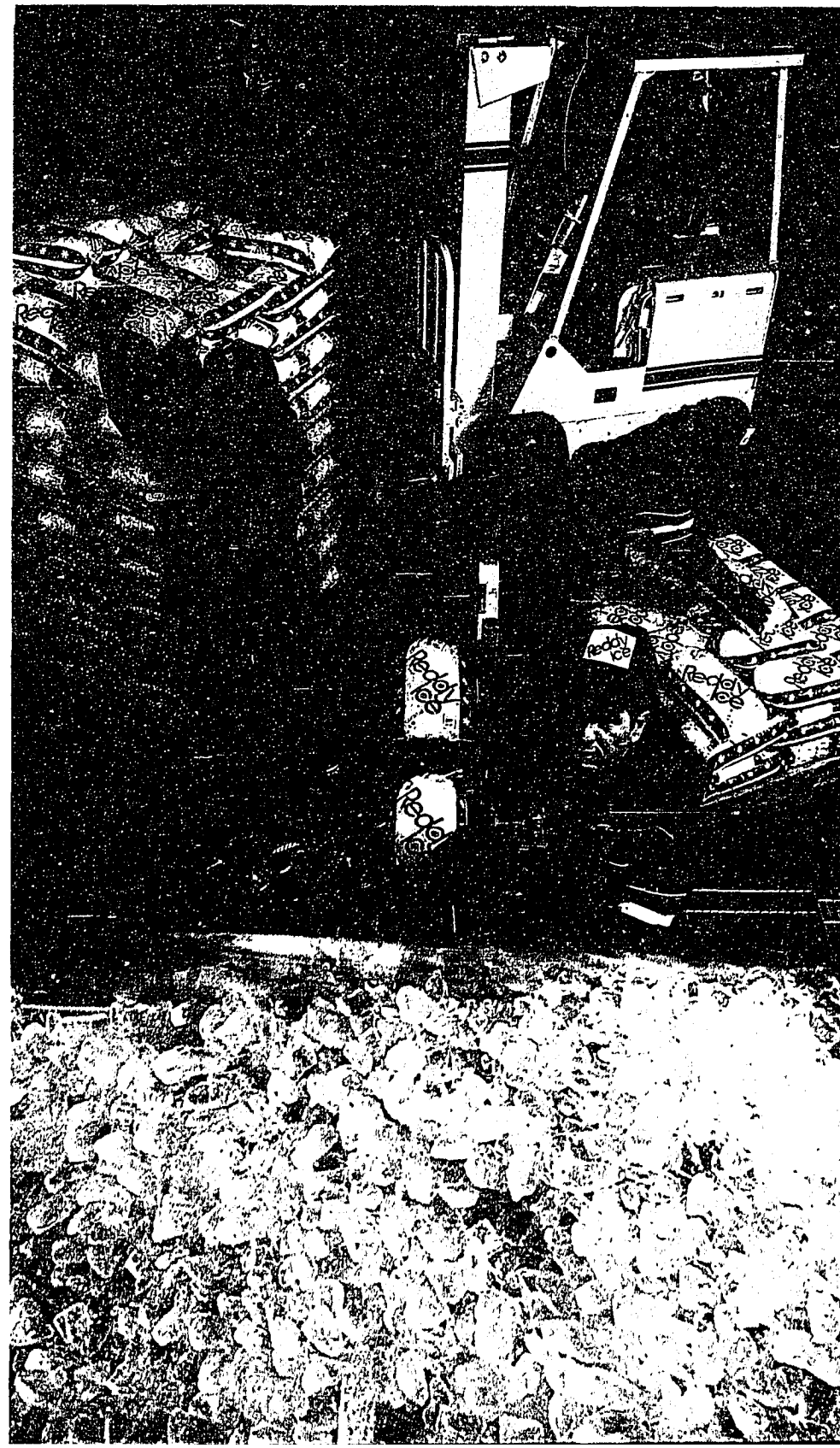
Tidel Systems' primary product is the "Timed Access Cash Controller" (TACC), a microprocessor-controlled, time-delayed dispensing system and drop safe specifically developed for use by cash-oriented retailers such as 7-Eleven. During the first part of 1981, Tidel was still affected by costs associated with the reengineering and retrofitting of certain components of the TACC II model. As a result of these modifications, demand for the TACC II unit improved as the year progressed. As an extension of its metal fabrication capabilities, the Division also began to produce and market specialized carts, dollies and similar equipment for other Southland operations and outside distributors and retailers.

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Much of 1981 was devoted to research and development of new products, which are scheduled for pre-production and market testing in 1982. The "Cashier" is a modular TACC designed to meet the multiple unit requirements of supermarkets and other large retailers. The "Energy Manager" is a microprocessor-based energy control and monitoring system which levels out peak-load demands for electrical power by energy-consuming equipment. Another product, the "RTU 80" remote-controlled telemetry unit, is installed at distant or hard-to-reach locations in oil and gas fields. It monitors the flow of natural gas and oil through pipelines and transmits the data to a central computer using either telephone or radio links.

Reddy Ice Exceeds Last Year

Following 1980's record results, Reddy Ice sales were up 5.1%, even though the demand for packaged ice was affected by last summer's unusually cool and wet weather conditions, particularly in Texas. With plants in Dallas, Waco, Houston, Austin, Ft. Lauderdale and Las Vegas, Reddy Ice has total annual production capacity of almost a half-million tons. Although about 65% of volume comes from its Texas markets, the Division also serves customers in Arizona, Arkansas, California, Colorado, Florida, Louisiana, Nevada and Utah. Outside customers accounted for 67% of sales.



The Dallas Reddy Ice plant is the largest fully automated ice manufacturing facility in the United States, packaging ice for 7-Eleven and other customers.

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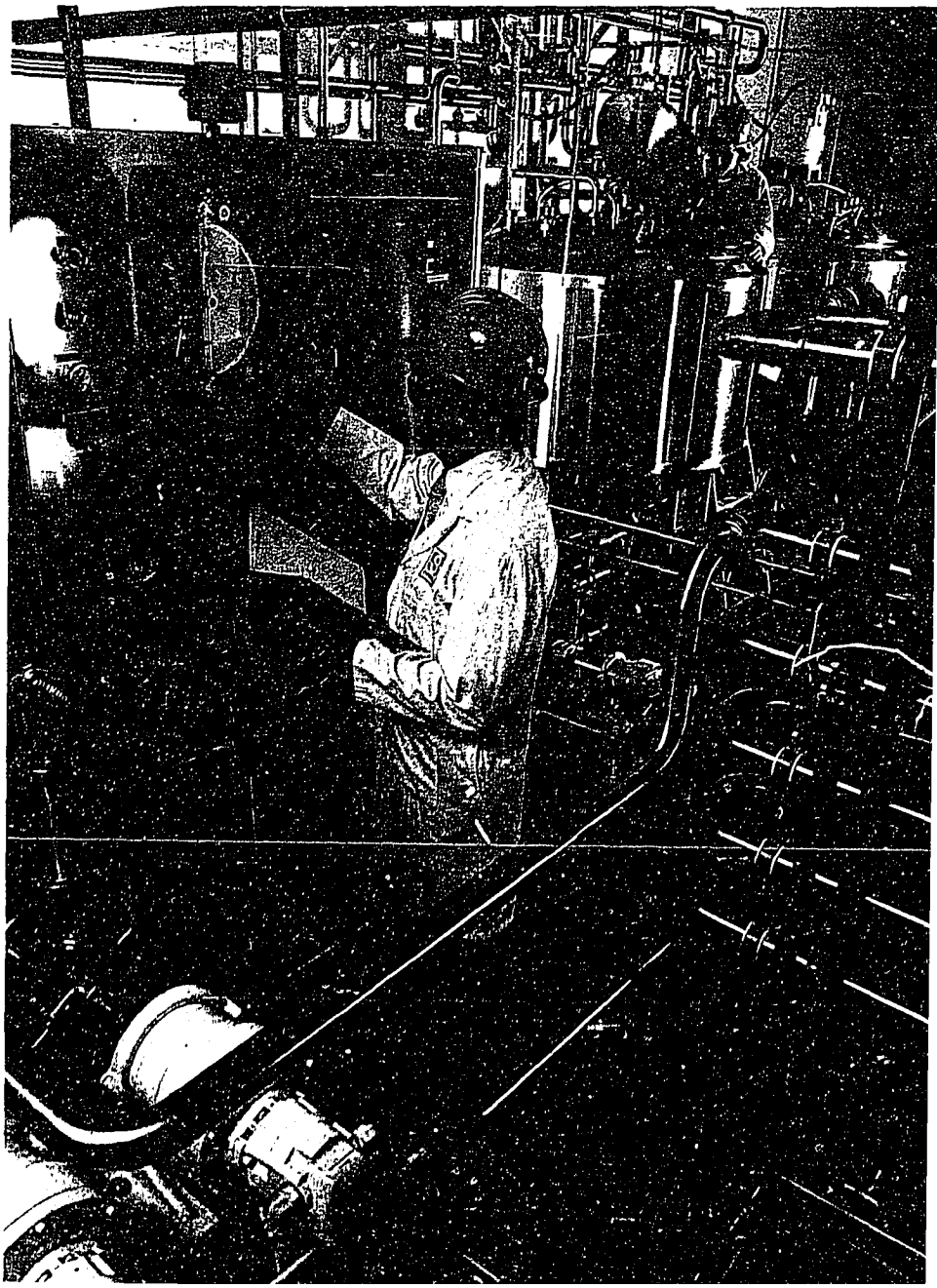
Chemical Emphasizes Food-Related Products

The Chemical Division produces a broad line of specialty chemicals for international and domestic customers, including Southland operations. Sales increased 3.2%, with outside accounts representing 83% of total volume.

The food ingredients plants in Dallas and Sanford, Florida, which together provide about 40% of the Division's sales, produce food flavorings, preservatives, emulsifiers, dough strengtheners and softeners, and other products used in the baking, bottling, pharmaceutical, dairy, food processing and animal feed industries. Intracompany sales include "Slurpee" flavor concentrates, dairy product flavorings, stabilizers, preservatives, cleansers and sanitizers.

During the year, the Division added an aseptic system to the Dallas plant to substantially increase processing capabilities for fruits and flavors used in ice cream, yogurt, pies and fruit toppings. The process produces fruit products that have a longer shelf life and achieve better color and flavor without the addition of artificial ingredients. It utilizes a closed system that rapidly heats the ingredients to very high temperatures, cools them quickly, then seals the finished product in airtight aluminum-poly bags for shipment.

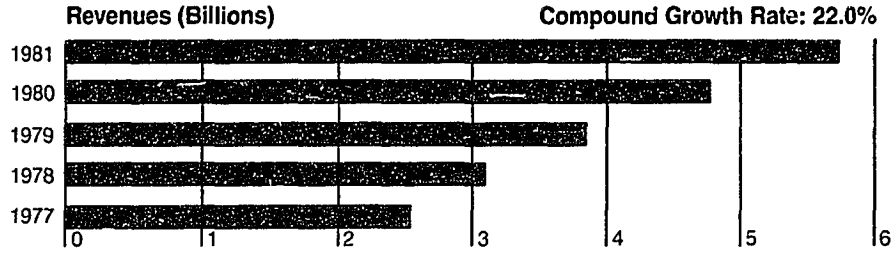
Three other plants in Dallas, Chicago and Great Meadows, New Jersey, manufacture non-food chemicals for numerous industrial applications. The Dallas operation produces cleansers, sanitizers, mirror-backing compounds, specialty coatings for appliance manufacturing and flexographic inks. The Chicago facility produces a wide range of compounds for industrial applications, such as sulfonated oils, phosphate esters, defoamers for chemical processing and leather tanning compounds. Continuing emphasis is being placed on developing and manufacturing metalworking and oil field services products, a new line which has significant growth potential for the Division. The Great Meadows plant produces chemicals for the pharmaceutical and agricultural industries, as well as products manufactured to customer specifications.



The Chemical Division completed installation during the year of an aseptic system to process fruits and flavors used in ice cream, yogurt and other products.

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FINANCIAL REVIEW



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SELECTED FINANCIAL DATA

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

	1981	1980	1979	1978	1977
			(Dollars in thousands except per share data)		
Operations (Notes 1 and 3)					
Net sales	**$5,693,636**	$4,758,656	$3,856,222	$3,076,532	$2,536,109
Other income	**40,524**	23,949	19,837	13,562	9,306
Total revenues	**5,734,160**	4,782,605	3,876,059	3,090,094	2,545,415
Increase over prior year	**19.90%**	23.39%	25.43%	21.40%	19.95%
Net earnings	**94,191**	76,052	81,251	56,213	44,589
Increase over prior year	**23.85%**	(6.40)%	44.54%	26.07%	19.95%
Per revenue dollar	**1.64%**	1.59%	2.10%	1.82%	1.75%
Return on beginning shareholders' equity	**17.29%**	15.53%	22.05%	17.30%	15.60%
Pro forma earnings (Note 2)	**94,191**	76,052	66,383	59,473	46,936
Increase over prior year	**23.85%**	14.57%	11.62%	26.71%	19.25%
Assets Employed (Notes 1 and 3)					
Working capital	**135,626**	174,966	147,057	125,313	122,234
Current ratio	**1.27**	1.44	1.46	1.46	1.57
Property, plant, and equipment including capital leases (net)	**964,860**	855,307	838,796	677,284	567,442
Depreciation and amortization	**101,095**	90,094	79,111	67,724	61,735
Total assets	**1,677,791**	1,495,385	1,367,575	1,134,476	942,531
Capitalization (Notes 1 and 3)					
Long-term debt	**320,918**	312,535	326,893	261,461	195,520
Capital lease obligations	**213,585**	224,753	226,257	211,342	192,547
Shareholders' equity	**615,021**	544,705	489,721	368,473	324,842
Total capitalization	**1,149,524**	1,081,993	1,042,871	841,276	712,909
Shareholders' equity to total capitalization	**53.50%**	50.34%	46.96%	43.80%	45.57%
Per Share Data (Notes 1, 3 and 4)					
Primary earnings	**3.98**	3.22	3.65	2.63	2.10
Earnings assuming full dilution	**3.86**	3.13	3.53	2.54	2.04
Pro forma primary earnings (Note 2)	**3.98**	3.22	2.98	2.78	2.21
Pro forma earnings assuming full dilution (Note 2)	**3.86**	3.13	2.89	2.69	2.14
Cash dividends	**1.05**	.91	.78	.64	.52
Shareholders' equity	**25.98**	23.04	21.99	17.21	15.30
Other Data					
Cash dividends	**24,859**	21,511	17,382	13,628	10,961
Dividends as a % of prior year net earnings (Note 1)	**32.69%**	26.47%	30.92%	30.56%	29.49%
Stock dividends	**—**	3%	3%	3%	3%
Average shares outstanding (Note 5)	**23,675,677**	23,640,048	22,274,263	21,410,955	21,234,456
Average diluted shares (Note 5)	**24,599,419**	24,583,510	23,267,942	22,416,583	22,308,757
Market price range (Note 5)					
High	**35**	29¼	30¼	31¾	24⅜
Low	**20½**	17	23⅝	20¼	18¼
Year-end	**31¾**	20½	27⅞	25¼	23⅛
Number of shareholders	**7,336**	8,429	8,708	8,627	8,764
Number of employees	**49,600**	46,800	44,300	37,000	34,000

Notes:

(1) 1977 has been restated for the change in the method of accounting for leases to comply with the provisions of Statement of Financial Accounting Standards No 13

(2) Earnings data for the years 1977 and 1978 have been restated to reflect the change in accounting for investment tax credits

(3) The years 1977 through 1980 have been restated to reflect the change in accounting for vacation pay

(4) Based on average shares outstanding adjusted for stock dividends

(5) Adjusted for stock dividends

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF *FINANCIAL CONDITION AND RESULTS OF OPERATIONS*

Accounting Information for the Three-Year Period 1979-1981:
Pro forma earnings for 1979 remove the cumulative effect of the accounting change made that year from the deferral to the flow-through method of accounting for investment tax credits (ITC) and present the year as if on the flow-through method. In 1981, the Company adopted Statement of Financial Accounting Standards No. 43 (SFAS No. 43) which requires an expense accrual for vacation time earned but not yet taken. The consolidated financial statements for 1980 and prior years have been restated to reflect this change.

RESULTS OF OPERATIONS:

Revenues
Revenues (net sales of products and merchandise, including sales by 7-Eleven stores operated by franchisees, and other income) established all-time highs in each of the past three years, with all business segments contributing to the gains.

Revenues (Millions)	1981	% Gain	1980	% Gain	1979	% Gain
Net Sales						
Stores Group	**$5,199.3**	**21.1**	$4,294.1	24.4	$3,453.0	24.0
Dairies Group	**368.2**	**2.7**	358.5	14.2	313.9	24.2
Special Operations Group	**126.1**	**18.9**	106.1	18.8	89.3	124.9
Total	**5,693.6**	**19.6**	4,758.7	23.4	3,856.2	25.3
Other Income	**40.5**	**69.5**	23.9	20.7	19.8	45.6
TOTAL	**$5,734.1**	**19.9**	$4,782.6	23.4	$3,876.0	25.4

The Stores Group accounted for 91.3%, 90.2% and 89.5% of total sales in 1981, 1980 and 1979, respectively. 7-Eleven volume, representing 83% of total sales, increased 19.1% to $4.73 billion in 1981, following gains of 23.7% to $3.97 billion in 1980 and 23.9% to $3.21 billion in 1979.

For 1981, 7-Eleven sales, excluding gasoline, were up 15.4% to $3.53 billion after increases of 15.8% and 17.9% in 1980 and 1979. These excellent gains resulted from sales increases substantially in excess of the rate of inflation in the 7-Eleven product mix and the net addition of 107, 90 and 206 7-Eleven stores in 1981, 1980 and 1979, respectively. More efficient use of selling space, increased prime-time television advertising, new products and services, and competitive pricing of selected items, especially milk, beer, cigarettes and soft drinks, contributed to the gains.

Self-serve gasoline, the largest single product category in the 7-Eleven sales mix, reached 25.3%, 23.0% and 17.2% of total convenience store sales in 1981, 1980 and 1979, respectively.

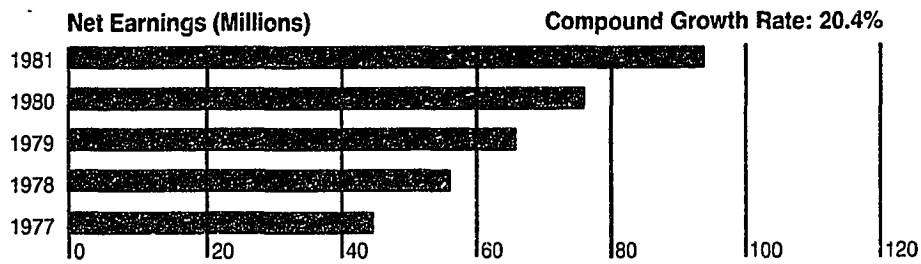
Gasoline	1981	% Gain	1980	% Gain	1979	% Gain
Sales (Millions)	**$1,195.4**	**30.9**	$912.9	60.4	$569.3	60.6
Gallons (Millions)	**956.0**	**20.6**	792 9	17.4	675.5	9.6
Number of Stores	**2,517**	**12.1**	2,246	6.6	2,107	13.5

Higher retail prices were largely responsible for the 1979 gasoline sales gain, although gallonage was up slightly, even in the face of a nationwide supply shortage. Although there were ample supplies in 1980, retail prices continued to escalate and were the main reason for the sales gain. In 1981, gallonage accounted for most of the sales gain as retail prices increased at a slower rate than in the prior two years due to continued ample nationwide supplies.

In December, 1981, the Company acquired certain gasoline storage facilities and formed a gasoline supply division whose primary purpose is to purchase and supply gasoline to the 7-Eleven retail operations. The division is expected to provide, either directly or through exchange arrangements, a major percentage of 7-Eleven's requirements nationwide at the lowest possible cost. In addition, it has allowed the Company to expand its wholesale gasoline business. Although this high-volume, low-profit product will lower overall corporate gross margins, Southland expects these activities to have a material effect on 1982 sales and earnings.

The Dairies Group accounted for 7% of Company sales in 1981 and 8% in 1980 and 1979. In 1981, sales were up only slightly due to increased competition in the marketplace and a reduction in government-sponsored school lunch and other social feeding programs. The 1980 and 1979 sales gains, which were in excess of the rate of inflation, resulted partly from an overall improvement in market conditions after the severe competitive environment of 1978. Increased

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☐ Earnings increased $15.7 million for cumulative effect of changing to flow-through method of accounting for ITC.

volume of milk, ice cream and related dairy products, the addition of new products and customers, and greater emphasis on the institutional food service market also contributed to the gains.

The Special Operations Group, including the Chief Auto Parts Division acquired at the end of 1978, represented 2% of total sales in each of the three years.

Other income (interest income, area license royalties, equity in earnings of affiliates and net gain on sale of assets no longer of use to the Company) is included in total revenues. Interest income and area license royalties represented more than 75% of other income in each year.

Gross Profits and Margins

Gross profits (sales less cost of goods sold, including buying and occupancy expenses) were up 15.9%, 15.5% and 21.8%, compared with sales gains of 19.6%, 23.4% and 25.3% in 1981, 1980 and 1979, respectively. For the same periods, gross margins (gross profits divided by sales) were:

Gross Margins (Percentage)			
QUARTERS	**1981**	1980	1979
First	**20.86**	21.81	22.91
Second	**22.92**	23.03	25.48
Third	**22.48**	23.38	24.79
Fourth	**20.64**	21.48	22.70
YEAR	**21.75**	22.46	24.00

7-Eleven gross margins, excluding gasoline, were up in each of the three years due largely to increased sales of high-margin products such as fountain soft drinks, fast foods, non-foods, candy and snack items. Although gasoline gross profits increased dramatically during the period, the impact of this low-margin item, as a larger percentage of the sales mix, caused both 7-Eleven and overall corporate margins to decline. In addition, margins have been adversely affected by inflation-fueled increases in buying and occupancy expenses including store rents and maintenance, utilities, inventory shortages and property taxes.

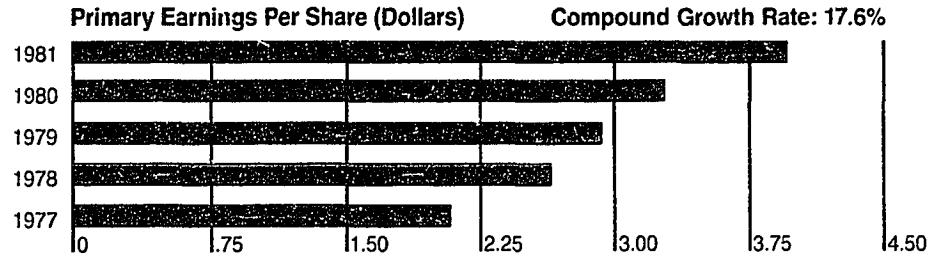
Dairies Group margins remained relatively stable in 1980 and 1979. While some markets continued to experience severe competition, generally favorable industry conditions, together with aggressive merchandising and promotions, introduction of new products, and processing efficiencies attributable to sustained plant modernization and automation programs, enabled the Group to maintain its margins. In 1981, an inability to pass through production cost increases due to competitive market conditions resulted in slightly lower gross margins.

Selling, General and Administrative Expenses

In 1981, 1980 and 1979, these expenses were up 16.1%, 15.4% and 27.0%, compared with gross profit gains of 15.9%, 15.5% and 21.8%, respectively. For the same periods, the ratios of these expenses to sales were:

Selling, General and Administrative Expenses (Percentage)			
QUARTERS	**1981**	1980	1979
First	**19.38**	20.13	20.86
Second	**18.40**	18.53	20.24
Third	**18.45**	19.07	20.06
Fourth	**17.53**	18.32	20.06
YEAR	**18.39**	18.96	20.27

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☐ Per share earnings increased 71¢ for cumulative effect of changing to flow-through method of accounting for ITC.

In 1979, the ratio increased .26 compared with the prior year, primarily due to the Company's decision to expand and upgrade field management and support staff in the areas of merchandising, gasoline procurement and marketing, real estate, construction, personnel, training, security and accounting. In addition, many inflation-fueled operating expenses, including wages and related payroll costs, travel and administrative expenses, increased at a faster pace than the growth in gross profits.

The Company, in late 1979, instituted numerous programs to bring this rate of growth in operating expenses more in line with that of gross profits. As a result, 1980 selling, general and administrative expenses were up 15.4%, compared with a 15.5% increase in gross profits. This improvement, as well as increased sales, resulted in the ratio of expenses to sales declining 1.31 to 18.96%. The Company has continued its cost reduction measures, and, in 1981, the ratio of selling, general and administrative expenses to sales declined .57 to 18.39%.

Interest and Imputed Interest Expense
Interest and imputed interest expense, which was up only 2.7% in 1981, increased 15.2% in 1980 and 14.5% in 1979 primarily because of unsecured debt financings in 1979 and 1978. Pursuant to SFAS No. 34, the Company reduced interest expense by the capitalization of $3.0 million, $3.5 million and $4.4 million of interest costs in 1981, 1980 and 1979, respectively.

Income Taxes
The effective federal and state income tax rates of 43.7% in 1981, 41.7% in 1980 and 40.4% in 1979 were substantially below the 46% federal statutory tax rate primarily because of investment tax credits. See Note 12 in Notes to Consolidated Financial Statements.

Net Earnings

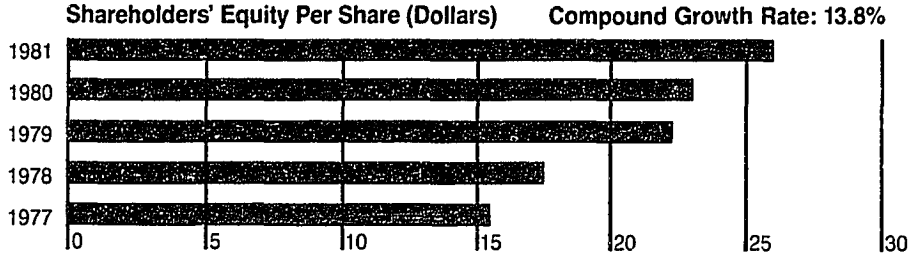
(Thousands)

QUARTER	1981	% Gain	1980	% Gain	1979*	% Gain
First	$ 7,685	35.4	$ 5,674	(10.1)	$ 6,309	(13.0)
Second	31,677	30.9	24,205	5.1	23,035	22.1
Third	31,832	19.5	26,629	10.7	24,049	21.7
Fourth	22,997	17.7	19,544	50.5	12,990	(4.5)
TOTAL	$94,191	23.9	$76,052	14.6	$66,383	11.6

*Pro forma

In 1979, the earnings increase was due largely to a 25.3% gain in sales, stable dairy market conditions and improved gross margins on both convenience store merchandise and self-serve gasoline. Total sales in 1980 continued strong, and although dairy and 7-Eleven margins, excluding gasoline, remained firm, the rate of increase in buying and occupancy expenses, as well as selling, general and administrative costs, held down the earnings gain. The increase in 1981 earnings was due to the excellent sales gain, a slight improvement in gross margins on convenience store merchandise, a decline in the ratio of selling, general and administrative expenses to sales, and a significant increase in interest income from short-term cash investments. The 1981 and 1980 earnings gains, however, were held down by operating losses from the Champaign Distribution Center and the Tidel Systems and Chief Auto Parts Divisions. These operations are expected to significantly improve their performance in 1982.

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Earnings Per Share

Primary

QUARTER	1981	% Gain	1980	% Gain	1979*	% Gain
First	$ .32	33.3	$ .24	(17.2)	$ .29	(14.7)
Second	1.34	31.4	1.02	(5.6)	1.08	22.7
Third	1.35	19.5	1.13	4.6	1.08	17.4
Fourth	.97	16.9	.83	56.6	.53	(17.2)
TOTAL	$3.98	23.6	$3.22	8.1	$2.98	7.2

*Pro forma

Primary earnings were computed on the basis of 23,675,677, 23,640,048 and 22,274,263 average shares outstanding for the years 1981, 1980 and 1979, respectively.

Diluted

QUARTER	1981	% Gain	1980	% Gain	1979*	% Gain
First	$ .32	33.3	$ .24	(17.2)	$ .29	(12.1)
Second	1.30	31.3	.99	(3.9)	1.03	21.2
Third	1.30	19.3	1.09	3.8	1.05	18.0
Fourth	.94	16.0	.81	55.8	.52	(16.1)
TOTAL	$3.86	23.3	$3.13	8.3	$2.89	7.4

*Pro forma

Diluted earnings were computed on the basis of 24,599,419, 24,583,510 and 23,267,942 average shares for the years 1981, 1980 and 1979, respectively.

The per share comparisons reflect the dilutive effect of two million shares sold in August, 1979, and 3% stock dividends in 1980 and 1979.

LIQUIDITY AND CAPITAL RESOURCES:

A company's liquidity is determined by its ability to generate adequate amounts of cash to meet both its short and long-term needs, through either internal or external sources. Due to the nature of Southland's business, approximately 85% of total sales are cash transactions, and receivables are rapidly converted into cash. In addition, the value of a substantial percentage of the inventories, determined by the LIFO method, is $52.6 million less than the FIFO cost of such inventories. As a result, Southland's internally generated funds from operations, supplemented by funds from external sources, are sufficient to meet its liquidity needs.

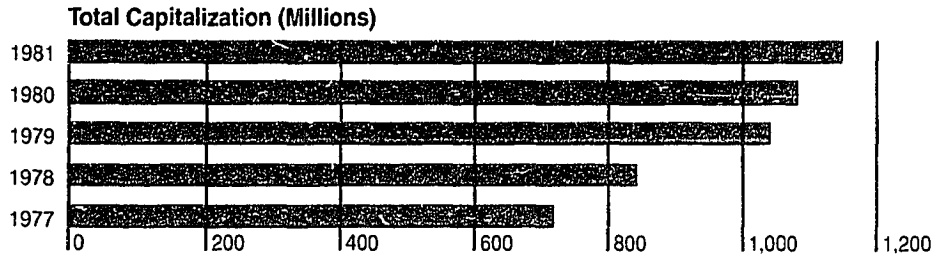
The following financial indicators also should be considered in evaluating Southland's liquidity:

	1981	1980	1979
Working Capital (Millions)	$135.6	$175.0	$147.1
Current Ratio	1.27	1.44	1.46
Inventory Turnover	12.4	11.6	10.8

Capital spending plans include major investments to strengthen the Company's position of leadership in the convenience store business and to develop and expand its other operations. In keeping with this program, investments in property, plant and equipment for the three-year period were:

(Millions)	1981	%	1980	%	1979	%
Stores Group	$165.0	74	$ 92.1	80	$180.9	81
Dairies Group	14.2	6	9.7	9	11.1	5
Special Operations Group	11.5	5	10.7	9	20.3	9
Corporate	33.2	15	2.0	2	10.7	5
TOTAL	$223.9	100	$114.5	100	$223.0	100

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Outlays for new 7-Eleven stores and sites, as well as remodeling and expanding existing facilities, reached an all-time high in 1979. To finance certain of these expenditures, the Company, in August, 1979, sold two million shares of common stock and $75 million 9½% unsecured debentures. In 1980, a significant reduction in capital expenditures was implemented due to unfavorable economic conditions, high interest rates and the establishment of more exacting 7-Eleven store site selection standards designed to improve return on investment. In 1981, Southland increased its capital expenditures primarily for 7-Eleven stores and sites, remodeling of existing facilities and for additional land and office buildings adjacent to the Corporate Office complex. The Company's financing requirements for its 1980 and 1981 capital spending programs were met from the 1979 financings and increased cash flow from operations.

During the past three years, internal sources have provided 50% of the funds required for capital expenditures and the increased working capital needed to support a higher level of sales.

During 1982 and 1983, Southland plans to continue its capital expenditures at or above 1981 levels, and anticipates both short and long-term financings. The Company, however, closely monitors and controls the level of its capital outlays and has the flexibility to adjust these expenditures as it did in 1980.

Southland utilizes both capital and operating leases and considers them to be valuable assets and essential to its operations. Capital lease obligations have changed only slightly during the period, as indicated below, although aggregate operating lease rentals have increased substantially. Southland plans to continue using both methods of lease financing.

The effect on the Company's capital structure of record earnings, dividends paid, capital leases, and equity and long-term debt financings completed during the period was:

(Millions)	1981	%	1980	%	1979	%
Long-Term Debt	$ 320.9	27.9	$ 312.5	28.9	$ 326.9	31.3
Capital Lease Obligations	213.6	18.6	224.8	20.8	226.3	21.7
Shareholders' Equity	615.0	53.5	544.7	50.3	489.7	47.0
TOTAL	$1,149.5	100.0	$1,082.0	100.0	$1,042.9	100.0

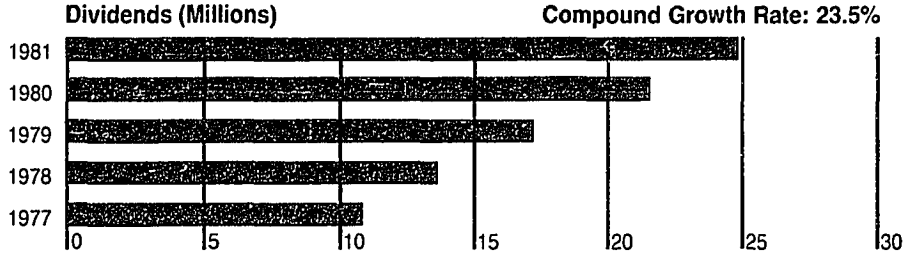
In summary, Southland's sound financial condition has allowed it to support its growth through the most advantageous combination of debt, equity and lease financing. The ratio of shareholders' equity to total capitalization has steadily improved during the period, and the ratio of long-term debt to total capitalization is an indicator of the Company's ability to enter the financial markets and obtain debt financing at acceptable rates.

The Company's public unsecured sinking fund debentures are rated "A" by both Moody's and Standard & Poor's. Its commercial paper is rated "P-2" by Moody's and was recently upgraded to "A-1" by Standard & Poor's.

EFFECTS OF INFLATION:

Refer to pages 27 and 28 — Supplementary Inflation Data (Unaudited).

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OTHER FINANCIAL DATA:

Dividends

The Company not only has followed a policy of reinvesting a major portion of net earnings to meet its growth objectives, but also has increased the annual cash dividend rate 10 times in the past 11 years. Cash dividends have been declared each of the past 25 years, and the annual rate has been raised 15 times.

Dividends Paid Per Common Share			
CASH:			
QUARTER	1981	1980	1979
First	$ .24	$.21	$.18
Second	.27	.24	.21
Third	.27	.24	.21
Fourth	.27	.24	.21
TOTAL	$1.05	$.93	$.81
STOCK:	—	3%	3%

In April, 1981, the annual dividend rate was increased 12.5% to $1.08 following gains of 14.3% to 96 cents in 1980 and 16.7% to 84 cents in 1979. In February, 1982, the Board of Directors increased the dividend 7.4% from $1.08 to $1.16, with the new rate effective the first quarterly payment in March.

Profit Sharing and Pension Plans

The Company contributes to The Southland Corporation Employees' Savings and Profit Sharing Plan, established in 1949, and to various union pension plans. Eligible employees have the option of joining Southland's voluntary contributory plan. Company contributions to this fully funded, trustee-administered plan are based on earnings before federal income taxes. All required contributions to such plans have been made.

Market Data

Southland's common stock is traded under the symbol SLC on the New York, Pacific, Boston and Philadelphia Stock Exchanges. The following market price and earnings per share information has been adjusted for 3% stock dividends in 1980 and 1979. The price/earnings ratios are based upon primary earnings per share for the four preceding quarters, using pro forma earnings for 1979 and 1978 only.

QUARTER	Price Range		Price/Earnings Ratio	
1981	High	Low	High	Low
First	**28⅜**	**20½**	**8.8**	**6.4**
Second	**27⅜**	**24⅛**	**8.3**	**7.3**
Third	**31⅛**	**24¾**	**8.6**	**6.8**
Fourth	**35**	**28½**	**9.1**	**7.4**
1980				
First	29¼	17¾	9.8	6.0
Second	22⅝	17	7.7	5.8
Third	24½	18⅞	8.5	6.6
Fourth	23¾	19	8.1	6.5
1979				
First	27⅝	23⅝	9.9	8.5
Second	27⅛	24⅛	9.9	8.8
Third	30¼	25⅝	10.3	8.7
Fourth	28⅞	24½	9.3	7.9

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SUPPLEMENTARY INFLATION DATA (UNAUDITED):

Introduction

Under generally accepted accounting principles, financial statements traditionally have been prepared on the basis of historical cost. Over time, inflation distorts this accounting measurement. Statement of Financial Accounting Standards No. 33 (SFAS No. 33) requires the presentation of supplementary financial information which attempts to show the impact of inflation. Because this information is experimental in nature, two different methods of presentation are required.

Methods of Measuring the Effects of Inflation

The first method provides information with respect to general inflation (constant dollar) by adjusting historical cost into dollars having the same purchasing power. For example, if the inflation rate is ten percent from one year to the next, then ten percent more dollars are needed in the second year to maintain the same purchasing power. SFAS No. 33 requires adjustment of certain historical financial data to constant dollars by using the Consumer Price Index for all Urban Consumers (CPI-U). Therefore, the historical cost of property, plant and equipment and of capital leases and related depreciation and amortization expense are adjusted using the CPI-U. Also, inventories and the related effect of inventories on cost of goods sold are similarly adjusted.

The second method provides information with respect to changes in specific prices (current cost) by adjusting historical cost to the cost which is currently required to purchase inventories and property, plant and equipment.

Over time, current cost increases at a rate different from the CPI-U. Current cost of property, plant and equipment and of capital leases and related depreciation and amortization expense were determined by application of appropriate published and internally developed indexes. The last-in, first-out (LIFO) method is used to determine the cost of the majority of inventories. Because of the rapid turnover of inventories and the use of LIFO, the cost of goods sold as shown in the historical cost financial statements approximates current cost. Current cost of inventories was estimated using first-in, first-out valuations adjusted for price changes through the end of the year.

Management's Comments

The following schedules compare financial data reported on a historical cost basis with data adjusted both for general inflation and for current cost.

Revenues (in millions of dollars) for 1981 were $5,734.2 and for 1977, expressed in average 1981 dollars, were $3,820.7, resulting in an average annual compound real sales growth rate from 1977 to 1981 of 11.1%.

Net earnings determined under the constant dollar and current cost methods are lower than earnings determined under the historical cost method. This decline results principally from the higher depreciation and amortization expense arising from significant inflationary increases in the cost of property, plant and equipment, and of capital leases. The impact of inflation on inventories is not significant since reported earnings are based on LIFO, which approximates the results obtained under the constant dollar and current cost methods.

Present tax laws do not allow deductions for depreciation adjusted for the effect of inflation. Therefore, the Company's tax rate based on data adjusted for the impact of inflation is in excess of the statutory rate. As shown in the following statement of earnings, the effective tax rate rises from 43.7% based on historical cost to 60.2% and 63.7% based on the general inflation and current cost methods.

The reduction in net earnings, discussed above, is more than offset by the unrealized gain from the decline in purchasing power of net amounts owed (monetary liabilities in excess of monetary assets). Since the monetary liabilities at year-end were larger than the monetary assets, a gain is shown. This gain represents the change in the amount of purchasing power required at year-end to pay these net liabilities versus the higher amount that would have been required to pay them at the end of the preceding year.

Selected Current Costs

The current costs of inventories and property, plant and equipment including capital leases, net of accumulated depreciation and amortization at December 31, 1981, and corresponding historical cost amounts, were as follows (Dollars in millions):

	Historical cost	Current cost
Inventories	$236.5	$ 289.2
Property, plant and equipment, including capital leases — net	964.9	1,537.3

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SUPPLEMENTARY INFORMATION — THE IMPACT OF GENERAL INFLATION AND SPECIFIC PRICE CHANGES ON SELECTED FINANCIAL DATA (Dollars in millions)

	Year ended December 31, 1981		
	As reported in financial statements	Adjusted for general inflation (constant dollar)	Adjusted for current cost
Revenues	$5,734.2	$5,734.2	$5,734.2
Cost of sales and expenses:			
Cost of goods sold, exclusive of depreciation and amortization	4,370.5	4,380.2	4,372.4
Depreciation and amortization	101.1	137.2	151.6
Interest expense, including imputed interest expense on capital lease obligations	47.6	47.6	47.6
Other operating expenses	1,047.6	1,047.6	1,047.6
	5,566.8	5,612.6	5,619.2
Earnings before income taxes	167.4	121.6	115.0
Income taxes	73.2	73.2	73.2
Net earnings	$ 94.2	$ 48.4	$ 41.8
Effective tax rate	43.7%	60.2%	63.7%
Unrealized gain from decline in purchasing power of net amounts owed		$ 60.2	$ 60.2
Increase in current cost of inventories, property, plant and equipment, and capital leases held during the year			$ 152.2
Effect of increase in general inflation			145.7
Excess of increase in current costs over increase in general inflation			$ 6.5

FIVE-YEAR COMPARISON OF SELECTED SUPPLEMENTARY FINANCIAL DATA ADJUSTED FOR EFFECTS OF CHANGING PRICES (IN AVERAGE 1981 DOLLARS) (Dollars in millions except per share data)

	Year ended December 31				
	1981	1980	1979	1978	1977
Revenues	**$5,734.2**	$5,278.7	$4,856.7	$4,307.6	$3,820.7
Historical cost information adjusted for general inflation:					
Earnings before cumulative effect of accounting change	**48.4**	42.7	52.1	—	—
Net earnings	**48.4**	42.7	71.7	—	—
Primary earnings per share:					
Before cumulative effect of accounting change	**2.04**	1.81	2.34	—	—
Net earnings	**2.04**	1.81	3.22	—	—
Net assets at year-end	**966.6**	983.9	931.2	—	—
Current cost information:					
Earnings before cumulative effect of accounting change	**41.8**	32.0	42.9	—	—
Net earnings	**41.8**	32.0	62.5	—	—
Primary earnings per share:					
Before cumulative effect of accounting change	**1.76**	1.35	1.93	—	—
Net earnings	**1.76**	1.35	2.81	—	—
Net assets at year-end	**1,141.5**	1,138.9	1,003.3	—	—
Excess of increase (decrease) in current cost over increase in general inflation	**6.5**	59.8	(75.0)	—	—
Unrealized gain from decline in purchasing power of net amounts owed	**60.2**	89.8	99.9	—	—
Cash dividends per common share	**1.05**	1.00	.98	.89	.77
Market price per common share at year-end	**31¾**	22⅜	34⅛	35	36
Average CPI-U	**272.4**	246.8	217.4	195.4	181.5

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MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The consolidated financial statements of The Southland Corporation and subsidiaries, as well as other financial information contained in this report, were prepared by management, which is responsible for their integrity and objectivity.

The Company's financial position and results of operations are presented in conformity with generally accepted accounting principles and, where appropriate, reflect estimates based on judgments of management. The Company has designed and implemented accounting and reporting systems and controls to provide reasonable assurance that transactions are accurately reflected on the books and records, assets are protected, established policies and procedures are followed, and the Company's financial position and results of operations are presented fairly. Accounting and reporting controls are monitored through an extensive program of internal audits by a professional staff of Company auditors which coordinates its activities with the Company's independent certified public accountants.

Touche Ross & Co. is engaged to examine the consolidated financial statements and issue their report thereon. Their examination is conducted in accordance with generally accepted auditing standards, including a review of internal controls and such tests of the accounting records as they consider necessary.

The Board of Directors, assisted by its Audit Committee of three non-employee directors, is responsible for assuring that management fulfills its responsibilities in the preparation of the financial statements and for recommending to shareholders the engagement of the independent certified public accountants, with whom the Committee reviews the scope of the audit and the accounting principles to be applied in financial reporting. The Committee meets as necessary, but at least three times a year. Touche Ross & Co. and the Company's internal auditors have direct access to the Committee — with or without the presence of management — to discuss any appropriate matter.

Clark J. Matthews, II
Executive Vice President
and Chief Financial Officer

TOUCHE ROSS & CO.

2001 Bryan Tower, Suite 2400
Dallas, Texas 75201

Board of Directors and Shareholders
The Southland Corporation
Dallas, Texas

We have examined the consolidated balance sheets of The Southland Corporation and subsidiaries as of December 31, 1981 and 1980, and the related consolidated statements of earnings, shareholders' equity, and changes in financial position for each of the three years in the period ended December 31, 1981. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the financial position of The Southland Corporation and subsidiaries at December 31, 1981 and 1980, and the results of their operations and the changes in their financial position for each of the three years in the period ended December 31, 1981, in conformity with generally accepted accounting principles consistently applied subsequent to January 1, 1979, the date of the change, with which we concur, in the accounting for investment tax credits as described in Note 12 to the consolidated financial statements, after restatement for the change, with which we concur, in the accounting for vacation pay as described in Note 2 to the consolidated financial statements.

Touche Ross & Co.
Certified Public Accountants

February 15, 1982

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CONSOLIDATED BALANCE SHEETS

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

ASSETS

	December 31 1981	December 31 (Dollars in thousands) 1980
Current Assets:		
Cash and short-term investments (Note 3)	**$ 141,770**	$ 149,602
Accounts and notes receivable (Note 4)	**162,449**	99,828
Inventories (Note 5)	**236,514**	213,445
Deposits and prepaid expenses (Note 12)	**32,862**	36,121
Investment in properties	**69,600**	77,900
Total Current Assets	**643,195**	576,896
Investments in Affiliates (Note 1)	**36,783**	31,777
Property, Plant, and Equipment (Note 6)	**774,968**	647,137
Capital Leases (Note 11)	**189,892**	208,170
Other Assets	**32,953**	31,405
	$1,677,791	$1,495,385

LIABILITIES AND SHAREHOLDERS' EQUITY

Current Liabilities:		
Accounts payable and accrued expenses (Notes 2 and 7)	**$ 463,920**	$ 354,729
Income taxes	**21,094**	22,368
Long-term debt due within one year (Note 8)	**6,147**	4,260
Capital lease obligations due within one year (Note 11)	**16,408**	20,573
Total Current Liabilities	**507,569**	401,930
Deferred Taxes (Notes 2 and 12)	**20,698**	11,462
Long-Term Debt (Note 8)	**320,918**	312,535
Capital Lease Obligations (Note 11)	**213,585**	224,753
Commitments for Operating Leases (Note 11)		
Shareholders' Equity (Notes 8 and 9):		
Common stock, $.01 par value, authorized 40,000,000 shares, issued and outstanding 23,683,182 and 23,643,903 shares	**237**	236
Additional capital	**335,294**	334,311
Retained earnings	**279,490**	210,158
	615,021	544,705
	$1,677,791	$1,495,385

See notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF EARNINGS

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

	Year ended December 31 (Dollars in thousands except per share data) 1981	1980	1979
Revenues:			
Net sales	**$5,693,636**	$4,758,656	$3,856,222
Other income	**40,524**	23,949	19,837
	5,734,160	4,782,605	3,876,059
Cost of Sales and Expenses:			
Cost of goods sold, including buying and occupancy expenses	**4,455,024**	3,689,912	2,930,693
Selling, general, and administrative expenses	**1,047,134**	902,286	781,768
Interest expense	**24,539**	23,841	18,746
Imputed interest expense on capital lease obligations	**23,048**	22,496	21,490
Contributions to Employees' Savings and Profit Sharing Plan (Note 10)	**16,965**	13,558	13,304
	5,566,710	4,652,093	3,766,001
Earnings Before Income Taxes	**167,450**	130,512	110,058
Income Taxes (Note 12)	**73,259**	54,460	44,472
Earnings Before Cumulative Effect in 1979 of Accounting Change for Investment Tax Credits	**94,191**	76,052	65,586
Cumulative Effect of Accounting Change for Investment Tax Credits (Note 12)	**—**	—	15,665
Net Earnings	**$ 94,191**	$ 76,052	$ 81,251
Earnings Per Share (Note 13):			
Earnings before cumulative effect of accounting change:			
Primary	**$3.98**	$3.22	$2.94
Fully diluted	**$3.86**	$3.13	$2.85
Net earnings:			
Primary	**$3.98**	$3.22	$3.65
Fully diluted	**$3.86**	$3.13	$3.53
Pro Forma Earnings, with accounting change in 1979 for investment tax credits applied retroactively (Note 12)	**$ 94,191**	$ 76,052	$ 66,383
Pro Forma Earnings Per Share (Note 13):			
Primary	**$3.98**	$3.22	$2.98
Fully diluted	**$3.86**	$3.13	$2.89

See notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

	Year ended December 31 (Dollars in thousands)		
Sources of Working Capital:	1981	1980	1979
From operations:			
Net earnings	$ 94,191	$ 76,052	$ 81,251
Expenses charged to earnings which did not require outlay of working capital:			
Depreciation and amortization	80,144	67,529	56,501
Amortization of capital leases	20,951	22,565	22,610
Deferred income taxes and other credits	9,236	7,884	(14,559)
Working capital provided from operations	204,522	174,030	145,803
Long-term debt	17,810	2,306	78,859
Retirements and sales of property, plant, and equipment	15,916	29,870	16,032
Capital lease obligations	9,446	24,011	30,476
Retirements and sales of capital leases	6,773	2,046	3,526
Issuance of common stock:			
Sale of stock	—	—	55,928
Other	984	517	1,564
	255,451	232,780	332,188
Uses of Working Capital:			
Property, plant, and equipment	206,864	114,510	217,087
Cash dividends	24,859	21,511	17,382
Reduction of capital lease obligations	20,614	25,515	22,261
Net noncurrent assets of businesses purchased	17,027	—	6,132
Capital leases	9,446	24,011	30,476
Payment of long-term debt	9,354	16,664	13,268
Investments in affiliates	5,006	2,930	1,483
Other	1,548	(344)	1,971
Retirement of long-term debt upon conversion of notes	73	—	270
Cash paid in lieu of fractional shares on stock dividend	—	74	114
	294,791	204,871	310,444
Increase (decrease) in working capital	$ (39,340)	$ 27,909	$ 21,744
Changes in Working Capital:			
Increases (decreases) in current assets:			
Cash and short-term investments	$ (7,832)	$ 69,675	$ (2,819)
Accounts and notes receivable	62,621	11,874	22,431
Inventories	23,069	12,651	29,315
Deposits and prepaid expenses	(3,259)	4,113	7,230
Investment in properties	(8,300)	10,400	11,643
	66,299	108,713	67,800
Increases (decreases) in current liabilities:			
Accounts payable and accrued expenses	109,191	64,616	67,092
Income taxes	(1,274)	15,742	(12,011)
Long-term debt due within one year	1,887	235	(9,230)
Capital lease obligations due within one year	(4,165)	211	205
	105,639	80,804	46,056
Increase (decrease) in working capital	$ (39,340)	$ 27,909	$ 21,744

See notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

	Year ended December 31 (Dollars in thousands)		
	1981	1980	1979
Common Stock:			
Balance, beginning of year	$ 236	$ 229	$ 202
Sale of stock	—	—	20
3% Stock dividend	—	7	7
Other	1	*	*
Balance, end of year	237	236	229
Additional Capital:			
Balance, beginning of year	334,311	319,067	242,340
Sale of stock	—	—	55,908
3% Stock dividend	—	14,727	19,255
Other	983	517	1,564
Balance, end of year	335,294	334,311	319,067
Retained Earnings:			
Balance, beginning of year:			
As previously reported			131,925
Effect of retroactive change in accounting for vacation pay (Note 2)			(5,994)
As restated	210,158	170,425	125,931
Net earnings for the year	94,191	76,052	81,251
Cash dividends	(24,859)	(21,511)	(17,382)
3% Stock dividend	—	(14,734)	(19,261)
Cash paid in lieu of fractional shares on stock dividend	—	(74)	(114)
Balance, end of year	279,490	210,158	170,425
Total Shareholders' Equity	$615,021	$544,705	$489,721

*Amount rounds to zero.
See notes to consolidated financial statements.

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THE SOUTHLAND CORPORATION AND SUBSIDIARIES

1 ACCOUNTING POLICIES:

Principles of Consolidation
The financial statements include the accounts of domestic and Canadian subsidiaries, all of which are wholly-owned. Intercompany transactions are eliminated.

Investments in affiliates are accounted for by the equity method. Accordingly, such investments are shown at cost to the Company plus equity in undistributed earnings since acquisition. Investments in affiliates consist primarily of amounts invested in a wholly-owned United Kingdom subsidiary engaged in the operation of retail stores. Equity in earnings of affiliates is included in other income and, as to foreign affiliates, is recorded net of amortization of the intangibles which arose on the acquisition (straight-line over 40 years), foreign income taxes, and a provision for United States federal income taxes. At December 31, 1981, the Company's equity in earnings of affiliates since date of investment was $7,163,000, and its investments in affiliates exceeded its equity in net assets by $18,540,000.

Revenues
Net sales are comprised of sales of products and merchandise, including sales by stores operated by franchisees.

Sales by stores operated under domestic and foreign area license agreements are not included. All fees or royalties arising from such agreements are included in other income. Initial fees are recognized as the services required under the agreements are performed.

Exchanges
Gasoline exchange receivables and payables, arising from the gasoline supply division (see Note 14), are included in trade accounts receivable and payable and result from exchange contracts in process. Exchange receivables are stated at the lower of the average cost of purchases or net realizable value. Exchange payables are stated at the higher of the average cost of purchases or prevailing market prices.

Inventories
Inventories are stated at the lower of cost or market, which, as to merchandise in stores, is determined by the retail inventory method. Cost is determined using the last-in, first-out (LIFO) method for substantially all inventories of the Stores Group and the first-in, first-out (FIFO) method for all other inventories.

Cost of inventories is primarily the purchase price of merchandise inventories.

Investment in Properties
Investment in properties includes land, buildings, and equipment either to be sold for cash and leased back or to be mortgaged, as well as closed stores held for sale. The Company expects that cash will be realized for these properties within a twelve-month period. Working capital is used in the acquisition, construction, and carrying of these assets.

Depreciation and Amortization
Depreciation of plant and equipment and amortization of capital leases are based upon the estimated useful lives of these assets using the straight-line method. Amortization of improvements to leased properties is based upon the remaining terms of the leases or the estimated useful lives of such improvements, whichever is shorter.

Income Taxes and Investment Tax Credits
Income taxes is the estimated amount of federal and state income taxes on earnings reported in the consolidated statements of earnings. Deferred taxes and deferred tax benefits are provided for and are a result of differences in timing between financial and tax reporting.

Investment tax credits are recorded as a reduction of income taxes in the year the related assets are placed in service.

Leases
Capital leases are recorded at the lower of the discounted present value of future lease payments or the fair value of the property. Provision is made for the present value of estimated losses anticipated to be incurred due to the payment of rentals on closed stores, net of expected sublease rentals.

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2 ACCOUNTING CHANGE — VACATION PAY:

On January 1, 1981, the Company adopted Statement of Financial Accounting Standards No. 43 (SFAS No. 43), which requires an expense accrual for vacation time earned but not yet taken. Accordingly, the consolidated financial statements for 1980 and prior years have been restated to comply with SFAS No. 43. The effect on the consolidated statements of earnings was as follows (000's omitted except per share data):

	1980	1979
Net earnings, as previously reported	**$77,672**	$83,141
Effect of retroactive accounting change	**(1,620)**	(1,890)
Net earnings, as restated	**$76,052**	$81,251
Effect on primary net earnings per share	**$(.07)**	$(.08)
Effect on fully diluted net earnings per share	**$(.06)**	$(.08)

3 CASH AND SHORT-TERM INVESTMENTS:

Cash and short-term investments include temporary cash investments of $131,033,000 and $142,185,000 at December 31, 1981 and 1980, stated at cost, which approximates market.

4 ACCOUNTS AND NOTES RECEIVABLE:

(000's omitted)	1981	1980
Trade accounts and notes receivable	**$127,335**	$ 75,354
Franchisee accounts receivable	**38,840**	30,052
	166,175	105,406
Allowance for doubtful accounts	**(3,726)**	(5,578)
	$162,449	$ 99,828

5 INVENTORIES:

Beginning in 1979, the Company changed from the FIFO to the LIFO method of determining the cost of substantially all inventories of the Stores Group because management believes this method more realistically reflects earnings during inflationary periods by matching the most recent inventory acquisition costs against current sales. At December 31, 1981 and 1980, inventories stated on the LIFO basis were approximately $178,379,000 and $155,737,000, which is less than FIFO cost (which approximates replacement cost) by approximately $52,587,000 and $38,576,000.

6 PROPERTY, PLANT, AND EQUIPMENT:

(000's omitted)	1981	1980
COST:		
Land	**$ 112,470**	$ 88,496
Buildings and leaseholds	**445,801**	369,020
Machinery and equipment	**455,904**	403,831
Vehicles	**66,495**	50,859
Construction in process	**32,261**	20,305
	1,112,931	932,511
Accumulated depreciation and amortization	**(337,963)**	(285,374)
	$ 774,968	$647,137

Approximately 17% of the carrying amount of property, plant, and equipment at December 31, 1981, was mortgaged. Lenders to certain wholly-owned real estate subsidiaries hold pledges of the shares of those subsidiaries as additional collateral.

Interest incurred to finance the construction or development of properties, which has been added to the cost of the related assets, was $2,961,000 in 1981, $3,539,000 in 1980, and $4,388,000 in 1979.

7 ACCOUNTS PAYABLE AND ACCRUED EXPENSES:

(000's omitted)	1981	1980
Trade accounts payable	**$295,594**	$208,708
Accrued payroll (Note 2)	**43,863**	37,612
Accrued taxes	**46,353**	33,876
Accrued interest	**7,922**	8,604
Other accounts payable and accrued expenses	**70,188**	65,929
	$463,920	$354,729

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8 LONG-TERM DEBT:

(000's omitted)	Amount outstanding	Due within one year	Balance included in long-term debt
5.75% — 15.75% Real estate, equipment, and other notes (mature 1982 to 2007)	$125,307	$ 6,147	$119,160
5% Convertible subordinated debentures due 1987	29,927	—	29,927
8⅜% Sinking fund debentures due 2002	47,500	—	47,500
9⅜% Sinking fund debentures due 2003	49,880	—	49,880
9½% Sinking fund debentures due 2004	74,451	—	74,451
	$327,065	$ 6,147	$320,918

The 5% convertible debentures may, at the option of the holders, be converted at any time prior to maturity into the Company's common stock. The present conversion ratio is 30.13 shares for each $1,000 of principal. At December 31, 1981, there were 901,700 shares reserved for the conversion of these debentures.

The 8⅜% debentures require annual sinking fund payments beginning February 15, 1983, in the amount of $2,500,000, which, at the option of the Company, may be increased each year by an additional amount not exceeding $2,500,000.

The 9⅜% debentures require annual sinking fund payments beginning December 15, 1984, in the amount of $2,500,000, which, at the option of the Company, may be increased each year by an additional amount not exceeding $2,500,000.

The 9½% debentures require annual sinking fund payments beginning August 15, 1985, in the amount of $3,750,000, which, at the option of the Company, may be increased each year by an additional amount not exceeding $5,625,000.

At December 31, 1981, the aggregate amounts of long-term debt maturities were as follows for the years ending December 31: 1982 — $6,147,000; 1983 — $8,035,000; 1984 — $10,496,000; 1985 — $14,564,000; 1986 — $15,081,000.

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9 STOCK OPTIONS AND KEY EMPLOYEES INCENTIVE PLAN:

Options under a nonqualified stock option plan are granted at the fair market value of the shares on date of grant and are exercisable ratably over a ten-year period. The proceeds from shares issued and any applicable tax benefits related to these options are credited to common stock and additional capital. No charges or credits are made to income with regard to options granted under this plan.

Information with respect to the nonqualified stock option plan is as follows:

	Number of shares reserved	Number of shares under option	Option price per share
Outstanding January 1, 1979	319,671	238,690	$19.10-$22.65
Granted	(2,652)	2,652	$26.16
Exercised	—	(1,109)	$19.10-$22.65
Outstanding December 31, 1979	317,019	240,233	$19.10-$26.16
Granted	—	—	
Exercised	—	—	
Outstanding December 31, 1980	317,019	240,233	$19.10-$26.16
Granted	(60,000)	60,000	$27.38
Exercised	—	(17,893)	$19.10-$22.65
Cancelled	19,416	(19,416)	$19.10-$22.65
Outstanding December 31, 1981	276,435	262,924	$19.10-$27.38

At December 31, 1981, 102,537 shares were exercisable at prices ranging from $19.10 to $27.38 and expire at various dates through April 22, 1991.

At December 31, 1981, 186,818 shares were reserved for issuance pursuant to a key employees incentive plan, of which approximately 40,000 shares will be issued in 1982. In 1981, 1980, and 1979, 24,827, 23,799, and 32,189 shares, respectively, were issued under this plan.

The above information has been adjusted for stock dividends.

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10 EMPLOYEES' SAVINGS AND PROFIT SHARING PLAN:

Effective January 1, 1949, the Company adopted The Southland Corporation Employees' Savings and Profit Sharing Plan (Profit Sharing) for the purpose of providing retirement benefits for eligible employees.

Contributions to the plan are made by both the participants and the Company. The Company contributes approximately 10% of its net earnings before contribution to the plan and federal income taxes. The Company contribution is allocated to the participants on the basis of their individual contribution, years of participation, and age.

11 LEASES:

Certain of the property and equipment used in the Company's business is leased. Generally, real estate leases are for primary terms of from 14 to 20 years with options to renew for additional periods, and equipment leases are for terms of from 5 to 10 years. The leases do not contain restrictions which have a material effect on the Company's operations.

The composition of capital leases reflected as assets in the consolidated balance sheets is as follows:

(000's omitted)	**1981**	1980
Buildings	**$276,478**	$277,500
Equipment	**85,844**	94,854
	362,322	372,354
Accumulated amortization	**(172,430)**	(164,184)
	$189,892	$208,170

Capital Lease Obligations
The present value of minimum lease payments for capital lease obligations of $229,993,000 at December 31, 1981, is reflected in the consolidated balance sheets as current and noncurrent capital lease obligations of $16,408,000 and $213,585,000, and represents the total minimum lease payments less estimated executory costs of $10,607,000 and an amount representing imputed interest of $218,375,000. Future minimum lease payments on these leases total $458,975,000 and are due in: 1982 — $38,644,000; 1983 — $36,838,000; 1984 — $34,771,000; 1985 — $32,781,000; 1986 — $30,132,000; and thereafter — $285,809,000.

The amount representing imputed interest necessary to reduce net minimum lease payments to present value has been calculated generally at the Company's incremental borrowing rate at the inception of each lease.

Operating Leases
Future minimum lease payments required by operating leases at December 31, 1981, total $550,892,000 and are due in: 1982 — $53,357,000; 1983 — $49,379,000; 1984 — $45,787,000; 1985 — $43,756,000; 1986 — $40,994,000; and thereafter — $317,619,000.

Lease expense on operating leases in the years ended December 31, 1981, 1980, and 1979, totaled $57,252,000, $47,034,000, and $36,961,000.

Leases with Profit Sharing
During 1981, 1980, and 1979, Profit Sharing purchased 108, 73, and 125 7-Eleven stores from the Company for $28,268,000, $18,769,000, and $26,606,000, the Company's direct and indirect cost. The stores were simultaneously leased to the Company at annual rentals approximating market rates. At December 31, 1981, Profit Sharing owned 993 stores leased to the Company under capital leases, which are included in property, plant, and equipment at a net amortized amount of $47,786,000, and 287 stores leased to the Company under operating leases.

12 INCOME TAXES:

Provisions for income taxes for the years ended December 31 are as follows:

(000's omitted)	**1981**	1980	1979
Currently payable:			
Federal	**$45,531**	$38,907	$37,203
Canadian	**3,662**	2,571	1,845
State	**9,190**	7,249	6,793
	58,383	48,727	45,841
Deferred	**14,876**	5,733	(1,369)
	$73,259	$54,460	$44,472

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Reconciliations of the Company's effective tax rate and the federal statutory rate for the years ended December 31 are as follows:

	1981	1980	1979
Federal statutory rate	**46.0%**	46.0%	46.0%
Investment tax credits	**(4.4)**	(5.2)	(8.6)
State income taxes net of federal income tax benefit	**2.9**	3.0	3.3
Other	**(.8)**	(2.1)	(.3)
	43.7%	41.7%	40.4%

The provisions for deferred income taxes for the years ended December 31 are as follows:

(000's omitted)	1981	1980	1979
Use of accelerated depreciation for tax purposes	**$8,532**	$5,141	$ 4,014
Other items	**6,344**	592	(5,383)
	$14,876	$5,733	$(1,369)

In 1979, the Company changed from the deferral to the flow-through method of accounting for investment tax credits. This change makes the Company's method of accounting for investment tax credits comparable with most other retailers and eliminates the future effects of continuing inflation on these credits. Pro forma earnings for 1979 reflect the results of operations for 1979 as if the Company had changed its accounting for investment tax credits in years previous to 1979.

Deferred taxes include deferred federal income taxes of $19,726,000 and $10,697,000 at December 31, 1981 and 1980. Net deferred tax benefits of $4,590,000 and $10,437,000 at December 31, 1981 and 1980, are included in deposits and prepaid expenses.

13 EARNINGS PER SHARE:

Primary earnings per share are based on the average number of shares outstanding during each year after giving effect to subsequent stock dividends.

Earnings per share assuming full dilution are based on (a) shares used in computing primary earnings per share, (b) shares issuable upon conversion of convertible debentures at the stated conversion rates (related interest requirements eliminated), (c) shares issuable on the exercise of stock options after reduction for shares assumed to have been purchased with the proceeds, and (d) average shares issuable under the key employees incentive plan.

14 GASOLINE SUPPLY DIVISION:

In early December 1981, the Company acquired certain storage facilities from a gasoline wholesaling company for $14,700,000, the fair market value. Gasoline exchange receivables (net of exchange payables) and inventory at their cost of $30,675,000, which the Company had previously purchased, as well as the facilities, were used to form a new gasoline supply division. These transactions were recorded under the purchase method of accounting, and operations, including exchange activities, are reflected in the Company's consolidated financial statements since the date of purchase. The unaudited pro forma financial information presented below combines the historical results of operations of the Company with the results of operations attributable to the assets purchased based on the hypothetical assumption that the purchases occurred on January 1, 1980, but is not necessarily indicative either of results that would have occurred had the purchases been effected on January 1, 1980, or of future results.

	Year ended December 31	
	(In millions except per share data)	
	1981	1980
Revenues	**$6,720**	$5,666
Net earnings	**108**	97
Net primary earnings per share	**4.54**	4.08

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15 QUARTERLY FINANCIAL DATA (UNAUDITED):

The classification of items in determining gross profit conforms to that used in the consolidated statements of earnings. Summarized quarterly financial data is as follows (000's omitted, except per share data):

	First quarter	Second quarter	Third quarter	Fourth quarter	Year
1981:					
Net sales	**$1,226,839**	**$1,438,975**	**$1,515,061**	**$1,512,761**	**$5,693,636**
Gross profit	**255,894**	**329,857**	**340,573**	**312,288**	**1,238,612**
Net earnings	**7,685**	**31,677**	**31,832**	**22,997**	**94,191**
Earnings per share:					
Primary	**.32**	**1.34**	**1.35**	**.97**	**3.98**
Fully diluted	**.32**	**1.30**	**1.30**	**.94**	**3.86**
1980:					
Net sales	$1,013,647	$1,201,176	$1,297,577	$1,246,256	$4,758,656
Gross profit	221,039	276,642	303,328	267,735	1,068,744
Net earnings	5,674	24,205	26,629	19,544	76,052
Earnings per share:					
Primary	.24	1.02	1.13	.83	3.22
Fully diluted	.24	.99	1.09	.81	3.13
1979:					
Net sales	$ 807,372	$ 956,301	$1,053,851	$1,038,698	$3,856,222
Gross profit	184,974	243,623	261,199	235,733	925,529
Earnings before cumulative effect of accounting change	5,512	23,035	24,049	12,990	65,586
Net earnings	21,177	23,035	24,049	12,990	81,251
Pro forma earnings	6,309	23,035	24,049	12,990	66,383
Earnings per share:					
Before cumulative effect of accounting change:					
Primary	.26	1.07	1.08	.53	2.94
Fully diluted	.25	1.04	1.04	.52	2.85
Net earnings:					
Primary	.99	1.07	1.07	.52	3.65
Fully diluted	.95	1.04	1.03	.51	3.53
Pro forma earnings:					
Primary	.29	1.08	1.08	.53	2.98
Fully diluted	.29	1.03	1.05	.52	2.89

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16 SEGMENT INFORMATION:

The Stores Group includes all convenience and grocery stores in the United States and Canada, as well as those activities (such as retail gasoline, distribution, and food preparation) which derive the majority of their revenues and operating profits from support of these stores, and the gasoline supply division. The Dairies Group includes milk and ice cream processing and distribution, salad-making, and packaging. The Special Operations Group includes the ice, chemical, Tidel, and Chief Auto Parts divisions. Corporate items reflect income, expenses, and assets not allocable to segments.

Intersegment sales are accounted for on a cost-plus-markup basis. Expenses directly identifiable with a segment and certain allocated expenses are used to determine operating profit by segment.

Segment information is as follows (000's omitted):

	1981	1980	1979
Revenues:			
Stores Group	**$5,229,369**	$4,307,876	$3,463,614
Dairies Group	**568,560**	534,699	473,367
Special Operations Group	**140,904**	122,645	113,919
Corporate	**7,725**	8,864	6,968
	5,946,558	4,974,084	4,057,868
Intersegment revenues:			
Dairies Group	**(198,329)**	(175,251)	(158,622)
Special Operations Group	**(14,069)**	(16,228)	(23,187)
Consolidated revenues	**$5,734,160**	$4,782,605	$3,876,059
Operating profits:			
Stores Group	**$ 221,610**	$ 174,171	$ 143,356
Dairies Group	**11,940**	14,015	9,687
Special Operations Group	**(9,346)**	(2,927)	7,385
Consolidated operating profits	**224,204**	185,259	160,428
Interest expense	**(47,587)**	(46,337)	(40,236)
Corporate expense — net	**(9,167)**	(8,410)	(10,134)
Consolidated earnings before income taxes	**$ 167,450**	$ 130,512	$ 110,058
Identifiable assets (including capital leases) at December 31:			
Stores Group	**$1,321,003**	$1,182,186	$1,045,898
Dairies Group	**122,583**	116,051	112,854
Special Operations Group	**97,230**	95,617	108,744
Corporate	**136,975**	101,531	100,079
Total identifiable assets	**$1,677,791**	$1,495,385	$1,367,575
Capital expenditures (excluding capital leases):			
Stores Group	**$ 165,001**	$ 92,112	$ 180,950
Dairies Group	**14,213**	9,656	11,126
Special Operations Group	**11,462**	10,712	20,269
Corporate	**33,215**	2,030	10,659
	$ 223,891	$ 114,510	$ 223,004
Depreciation and amortization expense:			
Stores Group	**$ 85,476**	$ 75,117	$ 60,822
Dairies Group	**7,930**	7,474	7,060
Special Operations Group	**4,538**	4,488	8,571
Corporate	**3,151**	3,015	2,658
	$ 101,095	$ 90,094	$ 79,111

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THE SOUTHLAND COMMITMENT



The "Southland family" participates in thousands of community projects in the neighborhoods we serve. Many activities are part of national fund raising programs which support research and medical services, including the Jerry Lewis Labor Day Telethon for the Muscular Dystrophy Association and the Mother's March on Birth Defects and Walk-America for the March of Dimes. MDA-sponsored summer camps in 38 states and Puerto Rico enable handicapped children to participate in activities such as wheelchair baseball, swimming, arts and crafts, nature study, and even a little clowning around.

BOARD OF DIRECTORS

JOHN P. THOMPSON (1948)
Chairman of the Board and
Chief Executive Officer

JERE W. THOMPSON (1961)
President

WILLIAM W. ATWELL* (1976)
Investments

J. Y. BALLARD (1937)
Consulting Engineer

WALTON GRAYSON, III (1962)
Executive Vice President

JOSEPH S. HARDIN (1977)
Retired Executive Vice President

MARK L. LEMMON, M.D.* (1977)
Plastic and Reconstructive
Surgeon

CLARK J. MATTHEWS, II (1981)
Executive Vice President

ALAN C. SCHOELLKOPF* (1979)
Vice President
Rotan Mosle Inc.

JODIE C. THOMPSON, JR. (1979)
Executive Vice President

CLIFFORD W. WHEELER (1960)
Retired Vice President

(Date indicates year elected)
*Members of Audit Committee

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SENIOR OFFICERS

John P. Thompson 56
Chairman of the Board and
Chief Executive Officer

Jere W. Thompson 49
President

Walton Grayson, III 53
Executive Vice President,
Administration and Services

Clark J. Matthews, II 45
Executive Vice President
and Chief Financial Officer

Jodie C. Thompson, Jr. 41
Executive Vice President,
Retail

S. R. Dole 44
Senior Vice President,
Stores Group

James W. Parker 43
Senior Vice President,
Manufacturing and Distribution

OPERATING OFFICERS

C. O. Beshears 55
Vice President,
Dairies Group

Donald L. Burnside 46
Vice President,
Western Stores Region

Adrian O. Evans 45
Vice President,
Central Stores Region

Joseph S. Hardin, Jr. 36
Vice President,
Distribution

Frank L. Kitchen 45
Vice President,
Eastern Stores Region

James R. Lynch 44
Vice President,
Southeastern Stores Region

Richard A. Turchi 47
Vice President,
International

Bill M. Wootton 43
Vice President,
Southwestern Stores Region

STAFF OFFICERS

Rulon R. Brough 58
Vice President,
Management Information
Services

M. T. Cochran, Jr. 63
Vice President

Vaughn R. Heady 61
Vice President

Ben M. Holland 49
Vice President,
Development

Bruce W. Krysiak 31
Vice President,
Marketing — Retail

P. Eugene Pender 50
Vice President
and Controller

L. Mark Rigg 48
Vice President,
Human Resources

John H. Rodgers 37
Vice President and
General Counsel

W. K. Ruppenkamp 62
Vice President

Henry T. Stanley, Jr. 45
Vice President,
Investor Relations

Forrest Stout 63
Vice President

Frank J. Gangi 40
Treasurer

R G Smith 58
Secretary

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SHAREHOLDER INFORMATION

SECURITIES LISTED:

New York Stock Exchange
Common Stock
8⅜% Sinking Fund Debentures
9⅜% Sinking Fund Debentures
9½% Sinking Fund Debentures

Luxembourg Stock Exchange
5% Convertible Subordinated Debentures

TRANSFER AGENT AND REGISTRAR:

First National Bank in Dallas
Common Stock

Mercantile National Bank in Dallas
8⅜% Sinking Fund Debentures

First International Bank in Houston, N.A.
9⅜% Sinking Fund Debentures
9½% Sinking Fund Debentures

AUDITORS:
Touche Ross & Co.
2001 Bryan Tower, Suite 2400
Dallas, TX 75201

ANNUAL MEETING:
The Annual Meeting of the Company will be held at 10 a.m. Wednesday, April 28, 1982, in the North Wing Auditorium of the Corporate Office, 2828 North Haskell Avenue, Dallas, Texas. All shareholders are cordially invited to attend.

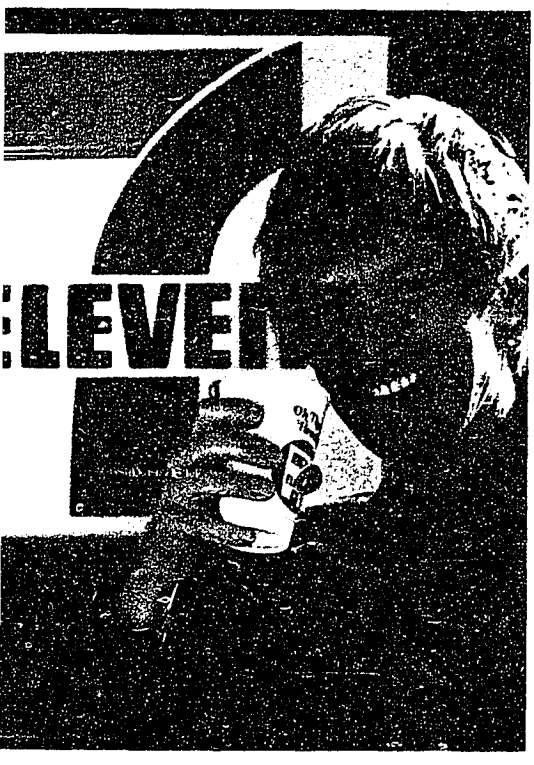
FORM 10-K:
Shareholders may obtain a copy, exclusive of exhibits, of the Form 10-K Annual Report for the year ended December 31, 1981, filed with the Securities and Exchange Commission, by writing to the Investor Relations Department at the Company's mailing address.

AUTOMATIC STOCK PURCHASE PLAN:
This plan provides a simple, convenient and inexpensive way for shareholders to invest cash dividends and additional cash deposits in Southland shares. For further information, write the Investor Relations Department at the Company's mailing address.

MAILING ADDRESS:
P.O. Box 719, Dallas, Texas 75221

TELEPHONE:
(214) 828-7011

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